

VERNON REDEVELOPMENT AGENCY
(A Component Unit of the
City of Vernon, California)

Annual Financial Report

For the Fiscal Year Ended June 30, 2008

VERNON REDEVELOPMENT AGENCY
For the Fiscal Year Ended June 30, 2008

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INDEPENDENT AUDITOR'S REPORT

Honorable Agency Governing Board
City of Vernon, California

We have audited the accompanying financial statements of the governmental activities and the major fund of the Vernon Redevelopment Agency (Agency), a component unit of the City of Vernon, California, as of and for the fiscal year ended June 30, 2008, 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 opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Agency's internal control over reporting. Accordingly, we express no such opinion. An audit also includes 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, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the major fund of the Agency as of June 30, 2008, and the respective changes in financial position thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 7 to the basic financial statements, the Agency adopted the provisions of Governmental Standards Accounting Board (GASB) Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, for the fiscal year ended June 30, 2008. The adoption of GASB Statement No. 53 required the Agency to restate beginning net assets at July 1, 2007.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 20, 2009, on our consideration of the Agency's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 8 is not a required part of the basic financial statements but is 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.

Macias Fini & O'Connell LLP
Certified Public Accountants

Los Angeles, California
January 20, 2009

REDEVELOPMENT AGENCY OF VERNON, CALIFORNIA
Management's Discussion and Analysis
(Unaudited)

As management of the Vernon Redevelopment Agency (the Agency), we offer readers of the financial statements this narrative overview and analysis of the financial activities of the Agency for the fiscal year ended June 30, 2008.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the Agency's basic financial statements. The Agency's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements.

Government-wide financial statements.

The *government-wide financial statements* are designed to provide readers with a broad overview of the Agency's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the Agency's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Agency is improving or deteriorating.

The *statement of activities* presents information showing how the Agency's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes).

The government-wide financial statements can be found on pages 9-10 of this report.

Fund financial statements.

A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Agency, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds.

Governmental funds are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

The smallest category of net assets with a balance of \$3,518,757 represents the Agency's restricted assets, which is restricted for payment of long-term debt.

The largest category of net assets with a balance of \$14,804,762 consists of \$35,425,632 of non-depreciable assets and \$6,010,330 of depreciable assets (net of depreciation) for a total of \$41,435,962, less the capital related debt of the Agency of \$26,200,000 in Industrial Redevelopment Project Tax Allocation Bonds issued in the prior years, less \$431,200 of bond premium (the pro-rata share of the premium related to debt used for capital purposes).

Changes in Net Assets

The table below summarizes the Agency's changes in net assets over the current and prior fiscal years. Details of the current year's changes in the net assets can be found on page 10 of this report.

VERNON REDEVELOPMENT AGENCY

Comparative Statements of Activities

For the Fiscal Years Ended June 30, 2008 and June 30, 2007

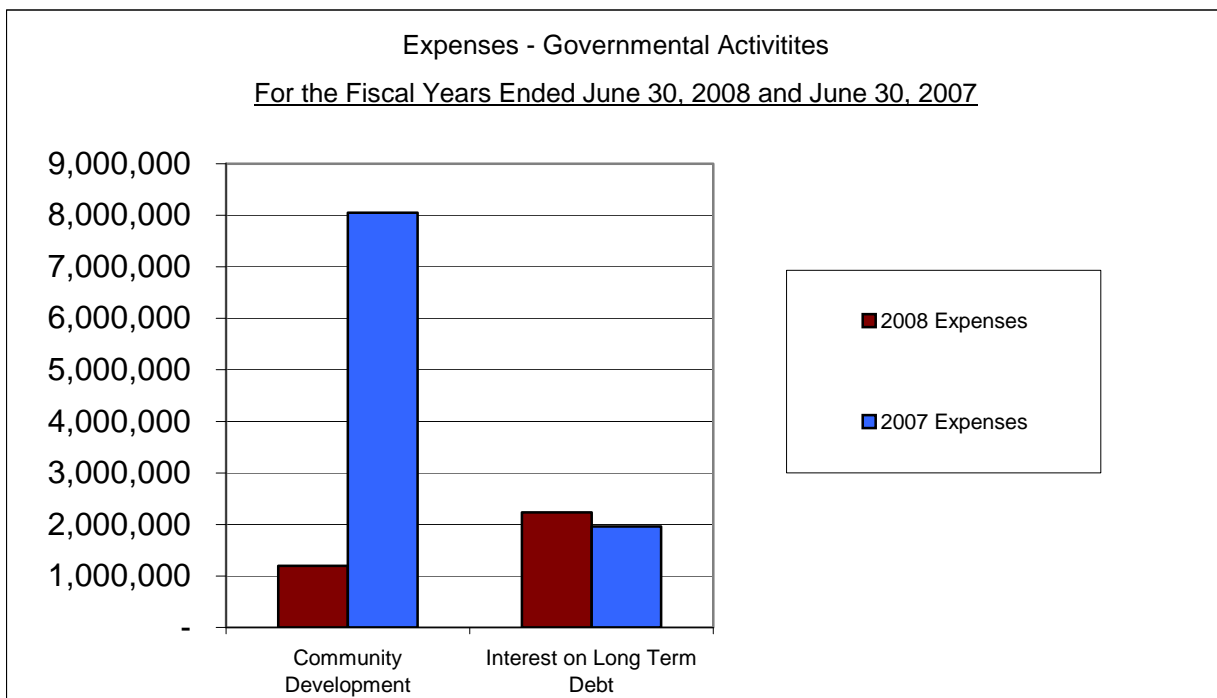
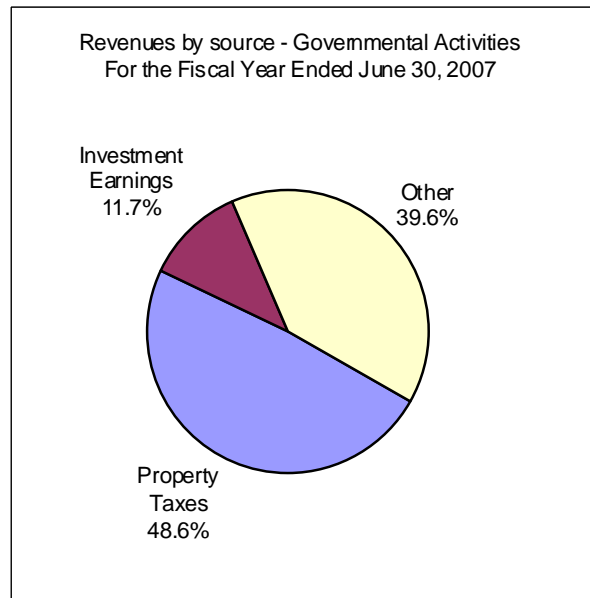
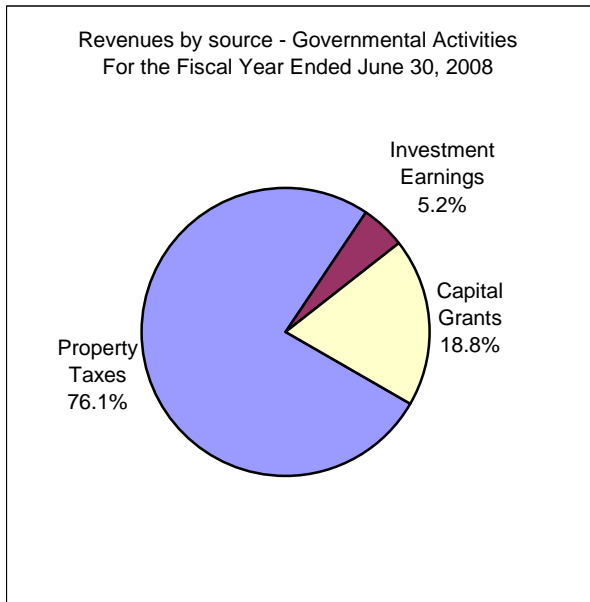
	2008	2007
	Governmental	Governmental
	Activities	Activities
	<u> </u>	<u> </u>
Revenues		
Program Revenues		
Capital grants and contributions	\$ 1,920,091	\$ -
General Revenues		
Taxes	7,789,207	7,668,705
Investment earnings*	529,990	1,847,253
Other revenues	<u>-</u>	<u>6,250,904</u>
Total revenues	<u>10,239,288</u>	<u>15,766,862</u>
Program Expenses		
Governmental activities:		
Community development	1,196,868	8,050,732
Interest on long-term debt	<u>2,232,245</u>	<u>1,962,574</u>
Total expenses	<u>3,429,113</u>	<u>10,013,306</u>
Increase in net assets	6,810,175	5,753,556
Net assets - beginning of year, restated (See Note 7)**	<u>21,170,798</u>	<u>15,672,984</u>
Net assets - end of year	<u>\$ 27,980,973</u>	<u>\$ 21,426,540</u>

*Includes investment income of \$463,510 and increase in fair value of derivative instruments of \$66,480.

**For comparative purpose, fiscal 2007 balances were not restated to reflect the Implementation of GASB Statement No. 53.

In the current year, the Agency's net assets increased by \$6,810,175. This is an increase of \$1,056,619 from the prior year. The key reasons for this increase in change in net assets are as follows:

- Revenues from investment earnings decreased \$1,317,263 from the prior year due to unfavorable market conditions.
- Other revenues decreased \$6,250,904 from the prior year mainly due to no gain recorded from the sale of land.
- However, program revenues increased \$1,920,091 and program expenses decreased \$6,584,193 from the prior year mainly due to federal and state awards earned in the current year and less redevelopment projects initiated in the current year.



FINANCIAL ANALYSIS OF THE GOVERNMENTAL FUNDS

As noted earlier, the Agency uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental fund.

The focus of the Agency's *governmental fund* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the Agency's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At the end of the current fiscal year, the Agency's governmental fund reported an ending fund balance of \$35,421,038, a decrease of \$15,344,885 in comparison with the prior year. Approximately 79% of the total fund balance amount, \$27,938,282, constitutes *unreserved fund balance*, which is available for spending at the Agency's discretion. Approximately 12% of the total fund balance amount, \$4,182,557, constitutes *reserved for debt service*, which is reserved for the repayment of debt. Approximately 8%, \$2,761,800 is *reserved for encumbrances*, which is reserved to liquidate contracts and purchase orders of the current period. The remainder of \$538,399 constitutes *reserved for redevelopment projects*, which is reserved for ongoing projects of the Agency.

At the end of the current fiscal year, the Agency's governmental fund reported total assets of \$38,360,853, a decrease of \$13,833,641 in comparison with the prior year. This decrease resulted from the use of escrow deposits to purchase land as a capital outlay.

At the end of the current fiscal year, the Agency's governmental fund reported total liabilities of \$2,939,815, an increase of \$1,511,244 in comparison with the prior year. The main reason for this increase was due to an increase in accounts payable for ongoing projects of the Agency.

For the current year, the Agency received \$120,502 more in tax revenues as compared to the prior year. This increase was due to increased assessed valuation on secured and unsecured properties.

For the current year, the Agency received \$1,383,743 less in investment earnings due to the Series 2005 Tax Allocation Bonds proceeds being spent for capital outlay.

For the current year, the Agency's intergovernmental revenues increased \$1,920,091 and redevelopment project expenditures decreased \$6,911,349 from the prior year mainly due to federal and state awards earned in the current year and less redevelopment projects initiated in the current year.

For the current year, the Agency's capital outlay was \$29,601,650 higher as compared to the prior year. The increase was due primarily to the purchase of land in the current year.

For the current year, the Agency's interest expenditures increased \$269,671 as compared to the prior year. This increase was mainly due to higher interest basis swap payments made in the current year (See Note 5 for additional information on basis swap).

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital assets.

The Agency's investment in capital assets for its governmental activities as of June 30, 2008, amounted to \$41,435,962 (net of accumulated depreciation). The net increase in investment in capital assets for the year was \$14,614,894 increase in land, \$7,488,454 increase in construction in progress, and \$195,896 increase in infrastructure (See Note 3 for additional information on capital assets).

There were no significant construction commitments outstanding as of June 30, 2008.

Outstanding debt.

Outstanding at June 30, 2008, were \$49,420,000 of Tax Allocation Bonds Series 2005. The Series 2005 Bonds were issued to (i) to finance various redevelopment projects in or benefiting the Agency's Industrial Redevelopment Project area, (ii) to fund the reserve requirement for the Series 2005 Bonds, and (iii) to pay costs of issuance related to the Series 2005 Bonds. As of June 30, 2008, \$538,399 of the debt proceeds is restricted and committed for future redevelopment projects.

As of June 30, 2008, all bonds issued by the Agency had an insured rating of AA by S&P and A2 by Moody's. However, during the Fiscal Year 2008 and subsequently thereafter, S&P and Moody's made numerous rating changes on the Agency bonds. Below is a summary of such rating changes.

- In June 2008, S&P downgraded the bond insurer MBIA, the bond insurer for the 2005 Series to AA from AAA. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to AA from AAA.
- In June 2008, Moody's downgraded the bond insurer MBIA, the bond insurer for the 2005 Series to A2 from Aaa. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to A2 from Aaa.
- In November 2008, Moody's downgraded the bond insurer to MBIA, the bond insurer for the 2005 Series to Baa1. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to Baa1.

Additional information on the Agency's long-term debt can be found in Note 4 of this report.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Agency's finances for all those with an interest in the Agency's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Finance, City of Vernon, 4305 Santa Fe Avenue, Vernon, California 90058.

VERNON REDEVELOPMENT AGENCY

Statement of Net Assets

June 30, 2008

	Governmental Activities
ASSETS	
Cash and investments	\$ 7,547,070
Restricted cash and investments	4,720,956
Interest receivable	7,683
Taxes receivable	201,230
Other assets	25,021,303
Bond issuance costs	2,210,390
Due from City	862,611
Capital assets:	
Nondepreciable	35,425,632
Depreciable, net	6,010,330
Total assets	<u>82,007,205</u>
LIABILITIES	
Accounts payable	2,939,815
Derivative liabilities	189,261
Long-term liabilities:	
Due within one year:	
Bonds interest payable	663,800
Bond premium	44,345
Due in more than one year:	
Bonds payable, net	50,189,011
Total liabilities	<u>54,026,232</u>
NET ASSETS	
Invested in capital assets, net of related debt	14,804,762
Restricted for debt service	3,518,757
Unrestricted	9,657,454
Total net assets	<u>\$ 27,980,973</u>

See accompanying notes to the basic financial statements.

VERNON REDEVELOPMENT AGENCY

Statement of Activities

For the Fiscal Year Ended June 30, 2008

	Expenses	Program Revenues Capital Grants and Contributions	Net Revenues (Expenses) and Changes in Net Assets Governmental Activities
FUNCTION/PROGRAM ACTIVITIES:			
Primary government:			
Community development	\$ 1,196,868	\$ 1,920,091	\$ 723,223
Interest on long-term debt	2,232,245	-	(2,232,245)
Total governmental activities	\$ 3,429,113	\$ 1,920,091	(1,509,022)
 GENERAL REVENUES:			
Property tax increment			7,789,207
Investment earnings			529,990
Total general revenues			8,319,197
 Change in net assets			 6,810,175
 NET ASSETS, BEGINNING OF YEAR, RESTATED			 21,170,798
 NET ASSETS, END OF YEAR			 \$ 27,980,973

See accompanying notes to the basic financial statements.

VERNON REDEVELOPMENT AGENCY

Balance Sheet
Governmental Fund
June 30, 2008

	Redevelopment Capital Projects Fund
ASSETS:	
Cash and investments	\$ 7,547,070
Restricted cash and investments	4,720,956
Interest receivable	7,683
Taxes receivable	201,230
Due from City	862,611
Other assets	25,021,303
Total assets	<u>\$ 38,360,853</u>
 LIABILITIES AND FUND BALANCE:	
Liabilities:	
Accounts payable	\$ 2,939,815
Total liabilities	<u>2,939,815</u>
Fund balance:	
Reserved for debt service	4,182,557
Reserved for redevelopment projects	538,399
Reserved for encumbrances	2,761,800
Unreserved	27,938,282
Total fund balance	<u>35,421,038</u>
Total liabilities and fund balance	<u>\$ 38,360,853</u>

See accompanying notes to the basic financial statements.

VERNON REDEVELOPMENT AGENCY
 Reconciliation of the Governmental Fund Balance Sheet to the
 Statement of Net Assets
 June 30, 2008

Fund balance-governmental fund (page 11)	\$ 35,421,038
 Amounts reported for governmental activities in the statement of net assets are different because:	
 Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental fund.	
Cumulative expenditures for capital assets, net of depreciation	41,435,962
 Other assets used in governmental activities do not consume current financial resources and therefore, are not reported in the governmental fund.	
Unamortized bond issuance cost	2,210,390
 Long-term liabilities are not due and payable in the current period and therefore are not reported in the governmental fund.	
Bonds payable	(49,420,000)
Bonds interest payable	(663,800)
Unamortized bond premium	(813,356)
Derivative liabilities	(189,261)
	(98,286,413)
Net assets of governmental activities (page 9)	\$ 27,980,973

See accompanying notes to the basic financial statements.

VERNON REDEVELOPMENT AGENCY
Governmental Fund
Statement of Revenues, Expenditures and Changes in Fund Balance
For the Fiscal Year Ended June 30, 2008

	Redevelopment Capital Projects Fund
REVENUES:	
Property tax increment	\$ 7,789,207
Intergovernmental revenues	1,920,091
Investment earnings	463,510
Total revenues	10,172,808
 EXPENDITURES:	
Redevelopment project costs	941,859
Capital outlay	33,888,668
Debt service:	
Interest payment on bonds	2,276,590
Total expenditures	37,107,117
Excess of expenditures over revenues	(26,934,309)
Other financing sources:	
Sale of property	11,589,424
Total other financing sources	11,589,424
 NET CHANGE IN FUND BALANCE	 (15,344,885)
 FUND BALANCE, BEGINNING OF YEAR	 50,765,923
 FUND BALANCE, END OF YEAR	 \$ 35,421,038

See accompanying notes to the basic financial statements.

VERNON REDEVELOPMENT AGENCY
Reconciliation of the Statement of Revenues, Expenditures, and
Changes in Fund Balance of Governmental Fund to the
Statement of Activities
For the Fiscal Year Ended June 30, 2008

Net change in fund balance - governmental fund (page 13) \$ (15,344,885)

Amounts reported for governmental activities in the statement of activities are different because:

The effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) is to decrease net assets.

Cost of property sold (11,589,424)

Governmental funds report capital outlay as expenditures. However, in the statement of net assets the cost of those assets is capitalized net of current year's depreciation expense.

Expenditures for capital assets	\$ 33,888,668	
Less current year depreciation	<u>(134,495)</u>	
		33,754,173

Governmental funds report the effect of issuance costs and premiums when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. In addition, the change in the fair value of the Agency's derivative, which does not qualify for hedge accounting, is reported in the statement of activities.

Change in unamortized bond issuance cost		(120,514)
Change in unamortized bond premium		44,345
Change in fair value of derivative liabilities		<u>66,480</u>

Change in net assets of governmental activities (page 10) \$ 6,810,175

See accompanying notes to the basic financial statements.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

The Vernon Redevelopment Agency (Agency) was activated September 16, 1986, by action of the Vernon City Council pursuant to the Community Redevelopment Law of California, as codified in Part I of Division 24 of the State of California Health and Safety Code. The Agency has the broad authority to acquire, rehabilitate, develop, administer, and sell or lease property. Additionally, the Agency has the right of eminent domain to facilitate acquisition of property. The Agency's Governing Board is the Vernon City Council.

The principal objectives of the Agency are to improve the commercial environment, provide new public improvements, strengthen the City of Vernon's (City) economic base, generate added employment opportunities, and expand the City's industrial base.

Since the City Council is the Agency's Governing Board, the Agency is considered to be an integral part of the City's reporting entity and has been included as a blended component unit in the City's basic financial statements for the fiscal year ended June 30, 2008. The Agency has no employees as all functions of the Agency are performed by the City.

Basis of Presentation

Government-wide Financial Statements

The statement of net assets and statement of activities display information about the Agency's activities. These statements include the financial activities of the Agency. These statements present the Agency's *governmental activities*, which normally are supported by taxes.

The statement of activities presents a comparison between program expenses and program revenues for each function of the Agency's governmental activities. Program expenses include such direct expenses that are specifically associated with a program or function and, therefore, are clearly identifiable as to a particular function. Program revenues include 1) charges paid by the recipients of goods or services offered by the programs and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented instead as general revenues.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Financial Statements

The fund financial statements provide information about the Agency's fund. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. The Agency reports one major governmental fund, the Redevelopment Capital Projects fund. This fund accounts for all revenues and expenditures related to operating the Agency in accordance with the California Community Redevelopment Law, including the acquisition of properties, cost of site improvements, other costs of benefit to the project, and general administrative expenditures incurred in sustaining Agency activities.

Basis of Accounting

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 at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the Agency gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied.

For the government-wide financial statements, the Agency applies all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board, the Accounting Principles Board or any Accounting Research Bulletins issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The Agency has elected to not apply private-sector standards issued after November 30, 1989.

Governmental fund type financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues and other governmental fund type financial resources are recognized when they become susceptible to accrual – that is, when they become both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon thereafter to pay liabilities of the current period. Property taxes and other revenue sources are considered available and are accrued when received within sixty days after fiscal year-end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due. General capital assets acquisitions are reported as expenditures in governmental fund statements.

Because the governmental fund financial statements are presented on a different measurement focus and basis of accounting than the government-wide financial statements, reconciliations are presented which briefly explains the adjustments necessary to reconcile the fund financial statements to the government-wide statements.

The Agency's policy regarding whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available is to use restricted resources first.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Capital Assets

Capital assets, which are reported in the government-wide financial statements, are recorded at historical cost or at estimated historical cost if actual historical cost is not available. The capitalization threshold for all capital assets is \$5,000. Capital assets used in operations are depreciated using the straight-line method over their estimated useful lives in the government-wide statements.

The estimated useful life is as follow:

Improvements other than building	40 years
Infrastructure	50 years

Maintenance and repairs are charged to operations when incurred. Betterments and major improvements, which significantly increase values, change capacities or extend useful lives, are capitalized. Upon sale or retirement of capital assets, the cost and related accumulated depreciation are removed from the respective accounts and any resulting gain or loss is included in the statement of activities.

Net Assets

The government-wide financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted and unrestricted.

- Invested In Capital Assets, Net of Related Debt – This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.
- Restricted Net Assets – This category presents external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.
- Unrestricted Net Assets – This category represents net assets of the Agency, not restricted for any project or other purpose.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Equity

In the fund financial statements, the governmental fund reports reservations of fund balance for amounts that are not appropriable or legally restricted for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

Property Taxes

The County of Los Angeles (County) levies, collects and apportions property taxes for all taxing jurisdictions within the County. Property taxes are determined by applying approved rates to the properties' assessed values. The County remits property taxes applicable to the Agency less an administrative fee throughout the year.

Article XIII A of the State of California Constitution limits the property tax levy to support general government services of the various taxing jurisdictions to \$1.00 per \$100 of assessed value. Taxes levied to service voter-approved debt prior to June 30, 1978 are excluded from this limitation.

Secured property taxes are levied in two installments, November 1 and February 1. They become delinquent with penalties on April 10 and December 10, respectively. The lien date is January 1 of each year for secured property taxes and the levy date occurs on the 4th Monday of September of the tax year.

Use of Estimates

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

NOTE 2 - CASH DEPOSITS AND INVESTMENTS

Cash and Investments

The Agency's cash and investments as of June 30, 2008 are classified in the accompanying financial statements as follows:

Cash and investments	\$ 7,547,070
Restricted cash and investments	<u>4,720,956</u>
Total cash and investments	<u><u>\$ 12,268,026</u></u>

The Agency's cash and investments as of June 30, 2008 consist of the following:

Deposits with financial institutions	\$ 147,070
Investments	<u>12,120,956</u>
Total cash and investments	<u><u>\$ 12,268,026</u></u>

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 2 - CASH DEPOSITS AND INVESTMENTS (CONTINUED)

The City's Investment Policy

The City's Investment Policy sets forth the investment guidelines for all funds of the City including the Agency. The Investment Policy conforms to the California Government Code Section 53600 et. seq. The authority to manage the City's investment program is derived from the City Council. Pursuant to Section 53607 of the California Government Code, the City Council annually appoints the City Treasurer and approves the City's investment policy. The Treasurer is authorized to delegate this authority as deemed appropriate. No person may engage in investment transactions except as provided under the terms of the Investment Policy and the procedures established by the Treasurer.

The Investment Policy requires that the investments be made with the prudent person standard, that is, when investing, reinvesting, purchasing, acquiring, exchanging, selling or managing public funds, the trustee (Treasurer and staff) will act with care, skill, prudence, and diligence under the circumstances then prevailing, including but not limited to, the general economic conditions and the anticipated needs of the City.

The Investment Policy also requires that when following the investing actions cited above, that the primary objective of the trustee be to safeguard the principal, secondarily meet the liquidity needs of depositors, and then achieve a return on the funds under the trustee's control. Further, the intent of the Investment Policy is to minimize risk of loss on the Agency's held investments from:

- A. Credit risk
- B. Custodial credit risk
- C. Concentration of credit risk
- D. Interest rate risk

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 2 - CASH DEPOSITS AND INVESTMENTS (CONTINUED)

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

The table below identifies the investment types that are authorized for the Agency by the California Government Code and the City's Investment Policy. The table also identifies certain provisions of the California Government Code that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investment of debt proceeds held by the bond trustee that are governed by the provisions of debt agreements of the Agency, rather than the general provisions of the California Government Code or the City's Investment Policy.

Authorized Investment Type	Maximum Maturity	Maximum Percentage of *Portfolio	Maximum Investment in One Issuer
Securities of the U.S. Government, or its agencies	None	None	None
Certain Asset-Backed Securities	None	None	None
Certificate of Deposit	None	30%	None
Bankers Acceptances	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20%	None
Medium-Term Notes	None	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
State Administered Pool Investment	N/A	None	None

* Excluding amounts held by bond trustee that are not subject to California Government Code restrictions.

Investments Authorized by Debt Agreements

Investments of debt proceeds held by the bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the City's Investment Policy. The table below identifies the investment types that are authorized for investments held by the bond trustee. The table also identifies certain provisions of these debt agreements that address interest rate risk, credit risk, and concentration of credit risk.

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
Securities of the U.S. Government, or its agencies	None	None	None
Certain Asset-Backed Securities	None	None	None
Certificate of Deposit	None	None	None
Bankers Acceptances	1 year	None	None
Commercial Paper	None	None	None
Money Market Mutual Funds	N/A	None	None
State Administered Pool Investment	N/A	None	None
Investment Contracts	None	None	None

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 2 - CASH DEPOSITS AND INVESTMENTS (CONTINUED)

Disclosure Relating to Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Agency manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. The Agency monitors the interest rate risk inherent in its portfolio by measuring the weighted average maturity of its portfolio. The Agency has no specific limitations with respect to this metric.

	Weighted Average Maturity (in years)	Fair Value as of June 30, 2008	% of Total
In custody of Treasurer:			
Deposits with financial institutions	-	\$ 147,070	1.95%
Investments held by Treasurer:			
Federal Home Loan Discount Notes	-	7,400,000	98.05%
Total in custody of Treasurer	-	7,547,070	100.00%
In custody of Trustee:			
Investments held by Trustee:			
Federal National Mortgage Association	4.47	3,622,500	76.73%
Money Market Mutual Fund	-	1,098,456	23.27%
Total in custody of Trustee	4.47	4,720,956	100.00%
Total cash and investments held by Treasurer and Trustee		\$ 12,268,026	

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 2 - CASH DEPOSITS AND INVESTMENTS (CONTINUED)

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by the California Government Code, the City's Investment Policy, or debt agreements, and the actual rating as of the year end for each investment type.

	Minimum Required Credit Rating	Actual Credit Rating Moody's/S&P	Fair Value as of June 30, 2008	% of Total
In custody of Treasurer:				
Deposits with financial institutions	Not Rated	Not Rated	\$ 147,070	1.20%
Investments held by Treasurer:				
Federal Home Loan Discount Notes	Not Rated	Not Rated	7,400,000	60.32%
Total in custody of Treasurer			7,547,070	61.52%
In custody of Trustee:				
Investments held by Trustee:				
Federal National Mortgage Association	Aaa / AAA	Aaa / AAA	3,622,500	29.53%
Money Market Mutual Fund	Aaa / AAA	Aaa / AAA	1,098,456	8.95%
Total in custody of Trustee			4,720,956	38.48%
Total cash and investments held by Treasurer and Trustee			\$ 12,268,026	100.00%

Concentration of Credit Risk

The City's Investment Policy places no limit on the amount the Agency may invest in any one issuer excluding a 10% limitation on commercial paper, mutual funds, and money market mutual funds. The City's Investment Policy also places no limit on the amount of debt proceeds held by a bond trustee that the trustee may invest in one issuer that are governed by the provisions of debt agreements of the Agency, rather than the general provisions of the California Government Code or the City's Investment Policy. As of June 30, 2008, the Agency's investments in any one issuer exceeding 5% were as follows:

	Issuer	In Custody of	Minimum Required Credit Rating	Actual Credit Rating Moody's/S&P	Fair Value as of June 30, 2008	% of Total
Federal Home Loan Discount Notes	Federal Home Loan Bank	Treasurer	Not Rated	Not Rated	\$ 7,400,000	60.32%
Federal National Mortgage Assn.	Federal National Mortgage Assn.	Trustee	Aaa/AAA	Aaa/AAA	3,622,500	29.53%
Money Market Mutual Fund	Invesco Aim	Trustee	Aaa/AAA	Aaa/AAA	1,098,456	8.95%

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 2 - CASH DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the City's Investment Policy do not contain legal or policy requirement that would limit the exposure to custodial credit risk for deposits or investments.

At year-end, the carrying amount of the Agency's deposits was \$147,070 and the bank balance was \$187,640. The difference between the bank balance and the carrying amount represents outstanding checks and deposits in transit. Of the bank balance, \$100,000 was covered by federal depository insurance and \$87,640 was collateralized by the pledging financial institution as required by Section 53652 of the California Government Code. Under the California Government Code, a financial institution is required to secure deposits in excess of \$100,000 made by state or local governmental units by pledging government securities held in the form of an undivided collateral pool. The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure Agency deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. Such collateral is held by the pledging financial institution's trust department or agent in the Agency's name.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 3 - CAPITAL ASSETS

Capital asset activity of governmental activities for the fiscal year ended June 30, 2008 was as follows:

	Balance June 30, 2007	Additions	Deletions	Transfers & Adjustments	Balance June 30, 2008
<i>Capital assets, not being depreciated:</i>					
Land	\$ 12,359,401	\$ 26,204,318	\$ -	\$ (11,589,424)	\$ 26,974,295
Construction in progress	962,883	7,684,350	-	(195,896)	8,451,337
Total capital assets, not being depreciated	<u>13,322,284</u>	<u>33,888,668</u>	<u>-</u>	<u>(11,785,320)</u>	<u>35,425,632</u>
<i>Capital assets, being depreciated</i>					
Building and Improvements	-	-	-	-	-
Improvements other than Building	12,523	-	-	-	12,523
Infrastructure	6,035,517	-	-	195,896	6,231,413
Total capital assets, being depreciated	<u>6,048,040</u>	<u>-</u>	<u>-</u>	<u>195,896</u>	<u>6,243,936</u>
Less accumulated depreciation for:					
Building and Improvements	(22,100)	-	-	22,100	-
Improvements other than Building	(313)	(313)	-	(156)	(782)
Infrastructure	(76,697)	(134,182)	-	(21,945)	(232,824)
Total accumulated depreciation	<u>(99,110)</u>	<u>(134,495)</u>	<u>-</u>	<u>(1)</u>	<u>(233,606)</u>
Total capital assets, being depreciated, net					
Building and Improvements	(22,100)	-	-	22,100	-
Improvements other than Building	12,210	(313)	-	(156)	11,741
Infrastructure	5,958,820	(134,182)	-	173,951	5,998,589
Total	<u>5,948,930</u>	<u>(134,495)</u>	<u>-</u>	<u>195,895</u>	<u>6,010,330</u>
Governmental activities capital assets, net	<u>\$ 19,271,214</u>	<u>\$ 33,754,173</u>	<u>\$ -</u>	<u>\$ (11,589,425)</u>	<u>\$ 41,435,962</u>

In the current year, the Agency purchased \$26,204,318 of land and sold \$11,589,424 of land to the City's Industrial Development Fund at cost for the City to development the land.

Depreciation

Depreciation expense of \$134,495 was charged to the community development function of the Agency.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 4 – LONG-TERM OBLIGATIONS

Outstanding at June 30, 2008, were \$49,420,000 of Industrial Redevelopment Project Tax Allocation Bonds Series 2005. The Series 2005 Bonds were issued to (i) to finance various redevelopment projects in or benefiting the Agency’s Industrial Redevelopment Project area, (ii) to fund the reserve requirement for the Series 2005 Bonds, and (iii) to pay costs of issuance related to the Series 2005 Bonds.

A summary of bonds payable is as follows:

Tax Allocation Bonds	Maturity	Interest Rates	Annual Principal Installments	Original Issue Amount	Outstanding at June 30, 2008
<i>Series 2005</i>	09/01/35	Fixed	To begin 09/01/09 - 09/01/35: \$1,160,000 - \$3,460,000	\$ 49,420,000	\$ 49,420,000
<i>Bond premium</i>				933,458	813,356
<i>Total Tax Allocation Bonds</i>				<u>\$ 50,353,458</u>	<u>\$ 50,233,356</u>

As of June 30, 2008, annual debt service requirements of the Agency to maturity are as follows:

Year ending June 30:	Industrial Redevelopment Project Tax Allocation Bonds Payable	
	Principal	Interest*
2009	\$ -	\$ 2,275,306
2010	1,160,000	2,256,456
2011	1,285,000	2,216,725
2012	1,380,000	2,171,694
2013	1,160,000	2,127,244
2014-2018	7,150,000	9,796,919
2019-2023	7,665,000	8,078,725
2024-2028	7,850,000	6,283,213
2029-2033	11,960,000	4,011,684
2034-2036	9,810,000	756,000
	<u>\$ 49,420,000</u>	<u>\$ 39,973,966</u>

* As of June 30, 2008, debt service was calculated at the actual fixed rates of the coupons ranging from 3.25% to 5.25%. See Note 5 for additional disclosure on basis swap.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 4 – LONG-TERM OBLIGATIONS (CONTINUED)

Changes in long-term liabilities

The following is a summary of long-term liabilities transactions for the fiscal year ended June 30, 2008:

	Balance June 30, 2007	Additions	Reductions	Balance June 30, 2008	Amounts Due Within One Year
Bonds payable	\$ 49,420,000	\$ -	\$ -	\$ 49,420,000	\$ -
Bond premium	857,701	-	(44,345)	813,356	44,345
	<u>\$ 50,277,701</u>	<u>\$ -</u>	<u>\$ (44,345)</u>	<u>\$ 50,233,356</u>	<u>\$ 44,345</u>

NOTE 5 – DERIVATIVE INSTRUMENT

As of June 30, 2008, the Agency has the following derivative instrument outstanding:

Type	Objective	Notional Amount	Effective Date	Maturity Date	Term	Fair Value
Basis Swap	Reduce interest cost on 2005 Series Bonds	\$ 49,420,000	March 2007	September 2035	Receive 67.073% of USD-ISDA ten year swap rate index, pay weekly average BMA	\$ (189,261)

Basis Swap – Series 2005

Objective of the interest rate swap: As a means to reduce its bond interest cost, the Agency entered into an interest basis swap in connection with its \$49,420,000 Industrial Redevelopment Project Tax Allocation Bonds, Series 2005 (the "Series 2005 Bonds").

Terms: As structured, the Series 2005 Bonds and the related swap agreement mature on September 1, 2035, and the swap's aggregate notional amount of \$49,420,000 matches the par amount of the Series 2005 Bonds. The swap was entered into on March 1, 2007. Under the swap, the Agency pays the counterparty payments equal to the average of the weekly Bond Market Association (BMA) variable rate index and receives payments equal to 67.073% of the USD-ISDA (ISDA) ten-year swap rate index.

Fair value: Because the differential between the BMA index and ISDA index has decreased since execution of the swap, the swap has an aggregate negative fair value of \$189,261 as of June 30, 2008. The fair value was estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 5 – DERIVATIVE INSTRUMENT (CONTINUED)

Credit risk: As the swap's fair value as of June 30, 2008 was negative, the Agency does not have credit exposure to the counterparty. Should the swap's fair value become positive, the Agency would have credit exposure to the counterparty equal to the fair value amount. The swap counterparty, Lehman Brothers, was rated A+ by Fitch Ratings and A1 by Moody's Investors Service as of June 30, 2008. To mitigate the potential for credit risk, if the counterparty's credit quality falls below "A-" or "A3", the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third-party custodian. See Note 6 for subsequent event disclosures regarding fair value of the swap and the bankruptcy of Lehman Brothers.

Basis risk: The swap exposes the Agency to basis risk should the relationship between ISDA index and BMA index diverge to a ratio lower than that stated in the swap. If such a change occurs, the swap may not provide the expected interest cost savings.

Termination risk: The Agency or its counterparty may terminate the swap if the other party fails to perform under the terms of the contract. The swap may be terminated by the Agency at any time. If at the time of termination, the swap has a negative fair value, the Agency would be liable to the counterparty for a payment equal to the swap's fair value.

Rollover risk. The Agency is not exposed to rollover risk since the term of the swap matches the term of the Series 2005 Bonds at the time of issuance.

The following summarizes the expected net debt service if BMA remains constant 1.55% and 10 Year ISDA remains constant at 4.75% (actual rates as of June 30, 2008).

Year Ending June 30	Principal Amount	Interest	Basis Swap, Net	Total Debt Service
2009	\$ -	\$ 2,275,306	\$ (808,495)	\$ 1,466,811
2010	1,160,000	2,256,456	(799,007)	2,617,449
2011	1,285,000	2,216,725	(779,007)	2,722,718
2012	1,380,000	2,171,694	(757,208)	2,794,486
2013	1,160,000	2,127,244	(736,431)	2,550,813
2014-2018	7,150,000	9,796,919	(3,348,498)	13,598,421
2019-2023	7,665,000	8,078,725	(2,729,734)	13,013,991
2024-2028	7,850,000	6,283,213	(2,121,604)	12,011,609
2029-2033	11,960,000	4,011,684	(1,325,134)	14,646,550
2034-2036	9,810,000	756,000	(247,358)	10,318,642
	<u>\$ 49,420,000</u>	<u>\$ 39,973,966</u>	<u>\$ (13,652,476)</u>	<u>\$ 75,741,490</u>

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Change in Fair Value of Derivative Instrument

The fair value balance and notional amount of the derivative instrument outstanding at June 30, 2008, classified by type, and the change in fair value of such derivative instrument for the year then ended as reported in the current year financial statements are as follows:

	Change in Fair Value		Fair Value at June 30, 2008		Notional
	Classification	Amount	Classification	Amount	
Governmental activities					
Hedging derivative instrument					
Cash flow hedge					
Basis Swap - Series 2005	Increase in fair value	\$ 66,480	Derivative liability	\$ (189,261)	\$ 49,420,000

The change in fair value adjusted to beginning net assets is discussed in Note 7. The change in fair value subsequent to June 30, 2008 is discussed in Note 6.

NOTE 6 – SUBSEQUENT EVENTS

Credit Rating

As of June 30, 2008, all bonds issued by the Agency had an insured rating of AA by S&P and A2 by Moody's. However, during the Fiscal Year 2008 and subsequently thereafter, S&P and Moody's made numerous rating changes on the Agency bonds. Below is a summary of such rating changes.

- In June 2008, S&P downgraded the bond insurer MBIA, the bond insurer for the 2005 Series to AA from AAA. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to AA from AAA.
- In June 2008, Moody's downgraded the bond insurer MBIA, the bond insurer for the 2005 Series to A2 from Aaa. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to A2 from Aaa.
- In November 2008, Moody's downgraded the bond insurer to MBIA, the bond insurer for the 2005 Series to Baa1. As a result of such rating action, the insured rating of the Agency 2005 Series was lowered to Baa1.

Change in Fair Value of Derivative Instrument

The fair value balance and notional amount of the derivative instrument outstanding at October 31, 2008, classified by type, and the change in fair value of such derivative instrument since June 30, 2008 are as follows:

	Change in Fair Value		Fair Value at October 31, 2008		Notional
	Classification	Amount	Classification	Amount	
Governmental activities					
Hedging derivative instrument					
Cash flow hedge					
Basis Swap - Series 2005	Decrease in fair value	\$ (1,076,851)	Derivative liability	\$ (1,266,112)	\$ 49,420,000

**VERNON REDEVELOPMENT AGENCY
NOTES TO BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

NOTE 6 – SUBSEQUENT EVENTS (CONTINUED)

On September 15, 2008, Lehman Brothers Holdings Inc. filed a petition in the United States Bankruptcy Court for the Southern District of New York seeking relief under Chapter 11 of the United States Bankruptcy Code. The Agency does not expect Lehman Brothers to be able to post collateral or to continue to perform its obligations under the Basis Swap in the future. The Agency is currently reviewing its procedures to terminate the Basis Swap – Series 2005 and determine any claims, if any, to be filed with the bankruptcy court.

NOTE 7 – IMPLEMENTATION OF GASB STATEMENT NO. 53

In the current year, the Agency adopted an early implementation of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. In accordance with GASB 53, an evaluation of effectiveness was performed on for the Agency's derivative instrument as of June 30, 2008 existing prior to July 1, 2007. The Agency's hedging derivative instrument was determined to be ineffective, accordingly, the derivative instrument was evaluated as of the end of the previous reporting period and reported as a restatement of beginning net assets.

For the governmental activities, the beginning net assets were restated by reducing beginning net assets by \$255,742, which was the fair value of the hedging derivative instrument determined to be ineffective as of the end of the previous reporting period.



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SAN DIEGO

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENT PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

Honorable Agency Governing Board
City of Vernon, California

We have audited the financial statements of the governmental activities and the major fund of the Vernon Redevelopment Agency (Agency), a component unit of the City of Vernon, California, as of and for the fiscal year ended June 30, 2008, which collectively comprise the Agency's basic financial statements and have issued our report thereon dated January 20, 2009. That report contained an explanatory paragraph describing the Agency's adoption of Governmental Accounting Standards Board (GASB) Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. 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 Agency's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Agency's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control over financial reporting.

A *control deficiency* 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 misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described below to be a significant deficiency in internal control over financial reporting

Finding

For the fiscal year ended June 30, 2008, we found instances where intergovernmental revenues were credited to redevelopment expenditures rather than being recorded and recognized as revenues in accordance with generally accepted accounting principles. This occurred because the Agency's system of internal control did not provide for a proper review and verification of the transactions to ensure proper accounting and recording.

Recommendation

Agency management should establish internal controls to ensure that all transactions are properly recorded and accounted for accurately.

Management Response

Agency management concurs with the finding and recommendation and has developed a corrective action plan to ensure all transactions are properly recorded and accounted for accurately.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, we consider the finding noted above to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Agency'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. 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's Office and as interpreted in the *Suggested Auditing Procedures for Accomplishing Compliance Audits of California Redevelopment Agencies*, issued by the Governmental Accounting and Auditing Committee of the California Society of Certified Public Accountants. 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*.

We noted certain matters that we reported to management of the Agency in a separate letter dated January 20, 2009.

The Agency's response to the finding identified in our audit is described above. We did not audit the Agency's response and accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Agency Board and management, others within the entity, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Macias Jini & O'Connell LLP
Certified Public Accountants

Los Angeles, California
January 20, 2009