

SANTA CRUZ METROPOLITAN TRANSIT DISTRICT

**FINANCIAL STATEMENTS
WITH
INDEPENDENT AUDITOR'S REPORT**

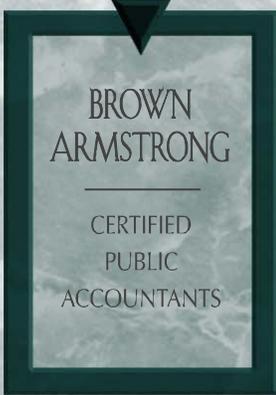
JUNE 30, 2012 AND 2011

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
JUNE 30, 2012 AND 2011**

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FINANCIAL SECTION



BROWN ARMSTRONG

Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Santa Cruz Metropolitan Transit District
Santa Cruz, California

We have audited the accompanying basic financial statements of the Santa Cruz Metropolitan Transit District (Santa Cruz METRO), as of and for the years ended June 30, 2012 and 2011. These basic financial statements are the responsibility of Santa Cruz METRO's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

We conducted our audits 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 audits to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Santa Cruz METRO, as of June 30, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2012, on our consideration of Santa Cruz METRO'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.

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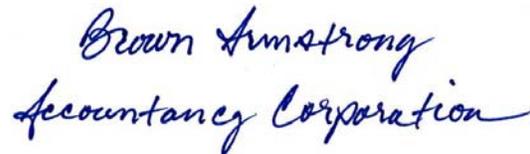


REGISTERED with the Public Company
Accounting Oversight Board and
MEMBER of the American Institute of
Certified Public Accountants

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedule of funding progress for Santa Cruz METRO's Defined Benefit Pension Plan and Other Postemployment Benefit (OPEB) Plan in the required supplementary information section be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements. The accompanying statements of operating expenses and the schedule of expenditures of federal awards are presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and are not a required part of the basic financial statements. The statements of operating expenses and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

A handwritten signature in blue ink that reads "Brown Armstrong Accountancy Corporation". The signature is written in a cursive, flowing style.

Bakersfield, California
December 20, 2012

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2012 AND 2011**

Introduction

This report provides a narrative and analytical overview of the financial activities of the Santa Cruz Metropolitan Transit District (Santa Cruz METRO) with selected comparative information for the years ended June 30, 2012 and 2011. This discussion has been prepared by management and should be read in conjunction with the basic financial statements and the notes thereto, which follow this section.

Santa Cruz METRO is an independent agency formed in 1969 by the legislature of the State of California for the purpose of providing transit service to the general public in Santa Cruz County (County). Santa Cruz METRO is governed by a Board of Directors composed of eleven directors, and one ex-officio director as described in Note 1.A.

The Financial Statements

Santa Cruz METRO's basic financial statements are prepared using proprietary fund (enterprise fund) accounting that uses the same basis of accounting as private-sector business enterprises. Santa Cruz METRO reports its financial results using one enterprise fund under the accrual method of accounting which records revenue when earned and expenses when incurred.

The Statement of Net Assets presents information on Santa Cruz METRO's assets and liabilities, with the difference between the two reported as net assets.

The Statement of Revenues, Expenses, and Changes in Fund Net Assets reports the operating revenues and expenses, non-operating revenues and expenses, and capital grant contributions. Federal capital grant expenses are listed in the Schedule of Expenditures of Federal Awards and are included in the current year increase in capital assets.

The Statement of Cash Flows reports the sources and uses of cash for the fiscal year resulting from *operating* activities, *non-capital* financing activities (operating grants and sales tax revenue), *capital* acquisitions and disposals, and related *financing* activities (non-transportation revenues). The net result of these activities, added to the cash balances at the beginning of the year, reconciles to the cash balances (current plus restricted) at the end of the current fiscal year on the Statement of Net Assets.

The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes describe the nature of Santa Cruz METRO's operations and significant accounting policies as well as clarify unique financial information.

Following the basic financial statements and footnotes is the Required Supplementary Information, which provides further detail on the funding progress of Santa Cruz METRO's defined benefit pension plan and other postemployment benefits.

The Statements of Operating Expenses, located in the Supplementary Information section of the financial statements, reports expenses in greater detail.

Financial Highlights

The management of Santa Cruz METRO is pleased to present the following discussion that provides an overview of the financial activities related to operations (operating revenue and expense) and capital funding (contributions) received for facilities improvements and the purchase of capital equipment for the year ended June 30, 2012.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2012 AND 2011**

In fiscal year 2012, Santa Cruz METRO received over \$6.9 million in capital grant contributions, a decrease of approximately \$3.6 million from the prior year. Depreciable capital asset additions for the year totaled approximately \$1.2 million net of disposals and retirements. Significant capital asset activity includes:

- Purchase of 11 forty-foot low-floor compressed natural gas (CNG) fixed route buses. Purchased with a Federal Transit Authority (FTA) "State of Good Repair" grant and funds from the California Transportation Commission's (CTC's) State Local Partnership Program (SLPP). – Project in progress.
- Installation of a new bus dispatching and transit management information technology system (Hastus/Giro). Funded with Federal Transit Administration (FTA) American Recovery and Reinvestment Act (ARRA) funds. – Project complete.
- Purchase and installation of an additional 15,000-gallon liquefied/compressed natural gas (L/CNG) storage tank at Santa Cruz METRO's existing Fueling Station. Funding for this second tank has been secured through a grant with the Monterey Bay Unified Air Pollution Control District (MBUAPCD), supplemented with funds from the Public Transportation Modernization, Improvement, and Service Enhancement Account (PTMISEA). – Project in progress.
- Design of the new Judy K. Souza Operations Facility began in late fiscal year 2012. The planned operations building and bus parking structure at 1200 River Street will provide a permanent state of the art facility from which to deploy the fixed-route fleet. This project is the final phase of the transit agency's MetroBase consolidated operations in the Harvey West area of Santa Cruz. The project budget is estimated at approximately \$26 million, with the majority of funding provided by the PTMISEA program, which was established through Proposition 1B. – Project in progress.
- Purchase of Land Mobile Radio equipment. Funding provided by the California Emergency Management Agency (CalEMA). – Project in progress.
- Bus stop improvements – funded with State Transportation Improvement Program (STIP) funds. – Project in progress.
- Upgrades to information technology software systems, including:
 - Human resources software, Spectrum/Epicor/iVantage
 - Fleet and facilities software, Maintstar
- Facilities repairs, replacements, and improvements, including:
 - Operations Building replacements – new dispatch counter
 - Pacific Station improvements – security fencing and concrete work
 - Renovation of Pacific Station – Lane 4 awning
 - Improvements to the Watsonville Transit Center, including installation of new automatic security doors
 - New emergency generator at Pacific Station

Santa Cruz METRO provided 5,463,380 rides on both its fixed-route and paratransit services this year.

As with many transit and public agencies across the region and throughout state, Santa Cruz METRO continues to face financial challenges due to significant increases in operating costs coupled with depressed revenues as a result of the lingering economic recession. In an effort to mitigate future projected budget deficits, in April 2011, the Board of Directors adopted a comprehensive strategy that included new revenue sources and expense reductions including a fare increase to local bus fares and a

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2012 AND 2011**

service reduction of 8.2% that was implemented in September 2011. Passenger fares were increased for the first time since 2003, while this was the second service reduction since 2010. Another component of the strategy adopted in April 2011 was the re-allocation and use of State Transit Assistance (STA) funding and Small Transit Intensive Cities (STIC) funds previously dedicated to Santa Cruz METRO's capital budget. With the re-allocations of these funding sources to the operating budget, it is expected that service will be fully restored following a complete and comprehensive system analysis that will begin in January 2013.

Future Outlook

Construction on the new Judy K. Souza Operations Facility will begin in fiscal year 2013 with funding provided by the PTMISEA program. This final phase of the Consolidated MetroBase project will bring operations, maintenance, and administration into one cluster of buildings and provide the needed infrastructure to achieve service expansion goals. Significant amounts of time and agency resources will be dedicated to this project over the next three years.

Additional future capital projects include:

- Re-design and remodel of the Watsonville Transit Center and Pacific Station in Santa Cruz
- Additions and upgrades to wireless internet equipment and service on-board the Highway 17 fleet
- Installation of second L/CNG storage tank at the existing River Street Fueling Station

Santa Cruz METRO continues its emphasis on better serving the public transportation needs of Santa Cruz County. In the Spring and Fall of 2012, service was increased to fill service deficits that occurred because of service reductions in previous years. Ongoing ridership analysis and transit planning studies will provide the data necessary to identify changes in the transit needs of riders for future service enhancements that will better serve the community in the coming years.

Statement of Net Assets:

	2012	2011	2010	2012 to 2011		2011 to 2010	
				Increase/(Decrease) Amount	%	Increase/(Decrease) Amount	%
Total Assets	\$ 122,760,286	\$ 107,633,960	\$ 105,530,289	\$ 15,126,326	14%	\$ 2,103,671	2%
Total Liabilities	\$ 39,859,087	\$ 20,233,981	\$ 22,352,299	\$ 19,625,106	97%	\$ (2,118,318)	-9%
Total Net Assets	\$ 82,901,199	\$ 87,399,979	\$ 83,177,990	\$ (4,498,780)	-5%	\$ 4,221,989	5%

Total Assets increased significantly this year due to increased restricted assets. Grant funds from PTMISEA for fiscal years 2010 and 2011 allocations were received in October 2011 and February 2012 totaling \$13,501,970. Additional capital grant funding was received from CalEMA in May and June 2012 in the amount of \$881,010. Funds received from PTMISEA will be spent on the Judy K. Souza Operations Facility, while funds received from CalEMA will be spent on the Video Surveillance and Land Mobile Radio projects.

Total Liabilities increased as well this year due to the receipt of the capital grant funds referenced above. These funds are restricted and reported as liabilities until spent on the specific project for which they were awarded.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2012 AND 2011**

For the fiscal year ended June 30, 2012, Santa Cruz METRO's net assets decreased by \$4,498,780.

Statement of Revenues, Expenses, and Changes in Fund Net Assets:

	2012	2011	2010	2012 to 2011		2011 to 2010	
				Increase/(Decrease) Amount	%	Increase/(Decrease) Amount	%
Operating Revenues	\$ 8,772,949	\$ 8,616,639	\$ 8,427,994	\$ 156,310	2%	\$ 188,645	2%
Operating Expenses	(47,296,458)	(44,621,709)	(42,629,146)	(2,674,749)	-6%	(1,992,563)	-5%
Operating Loss	(38,523,509)	(36,005,070)	(34,201,202)	(2,518,439)	-7%	(1,803,868)	-5%
Non-Operating Revenues	27,085,055	29,757,700	24,327,789	(2,672,645)	-9%	5,429,911	22%
Capital Grant Contributions	6,939,674	10,469,359	6,861,247	(3,529,685)	-34%	3,608,112	53%
Increase (Decrease) in Net Assets	<u>\$ (4,498,780)</u>	<u>\$ 4,221,989</u>	<u>\$ (3,012,166)</u>	<u>\$ (8,720,769)</u>	<u>-207%</u>	<u>\$ 7,234,155</u>	<u>-240%</u>

Operating Revenues (Passenger Fares) increased by 1.81% this year due to an increase in local fares effective September 2011. The last time local fares were increased was July 2003.

Operating Expenses increased by 5.99% overall when compared to last year due to increases in medical insurance rates, the California Public Employees' Retirement System (CalPERS) retirement rate, workers' compensation costs, and legal claims settlement costs.

Non-Operating Revenues decreased by 8.98% primarily due to the use of the 2011 STA allocation in the operating budget, while the 2012 STA allocation will be used in the capital budget to fund the Judy K. Souza Operations Facility.

Capital Contributions are capital grant funds received for facilities improvements and the purchase of capital equipment including revenue vehicles. The receipt of capital grant funds can fluctuate year over year based on a variety of factors including project eligibility requirements, formula-based funding criteria, the economy, etc. Capital contributions decreased by 33.71% from the prior year as one-time grant funding was received in 2011 under ARRA.

Statement of Cash Flows:

	2012	2011	2010	2012 to 2011 Change	2011 to 2010 Change
Net Cash Used in Operating Activities	\$ (31,551,498)	\$ (30,548,418)	\$ (30,988,599)	\$ (1,003,080)	\$ 440,181
Net Cash Provided by Non-Capital Financing Activities	27,233,074	28,867,864	24,074,716	(1,634,790)	4,793,148
Net Cash Provided by (Used in) Capital and Related Financing Activities	20,133,373	(1,091,853)	(637,360)	21,225,226	(454,493)
Net Cash Provided by Non-Transportation Activities	158,886	260,260	318,624	(101,374)	(58,364)
Net Increase (Decrease) in Cash and Cash Equivalents	15,973,835	(2,512,147)	(7,232,619)	18,485,982	4,720,472
Cash and Cash Equivalents, Beginning of Year	26,688,958	29,201,105	36,433,679	(2,512,147)	(7,232,574)
Cash and Cash Equivalents, End of Year	<u>\$ 42,662,793</u>	<u>\$ 26,688,958</u>	<u>\$ 29,201,060</u>	<u>\$ 15,973,835</u>	<u>\$ (2,512,102)</u>

Cash and cash equivalents held by Santa Cruz METRO increased by \$15,973,835 or 59.9% during the current year.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
JUNE 30, 2012 AND 2011**

Contacting Santa Cruz METRO's Financial Management

Santa Cruz METRO's financial report is designed to provide Santa Cruz METRO's Board of Directors, management, and the public with an overview of Santa Cruz METRO's finances. For additional information about this report, please contact Angela Aitken, Finance Manager, at 110 Vernon Street, Santa Cruz, CA 95060.

BASIC FINANCIAL STATEMENTS

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF NET ASSETS
JUNE 30, 2012 AND 2011**

<u>ASSETS</u>	<u>2012</u>	<u>2011</u>
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 25,241,660	\$ 22,771,455
Sales Tax, Grants, and Other Receivables	5,091,540	6,551,495
Inventory	730,930	816,327
Prepays	101,586	304,136
	<u>31,165,716</u>	<u>30,443,413</u>
RESTRICTED ASSETS		
Cash and Cash Equivalents	<u>17,421,133</u>	<u>3,917,503</u>
CAPITAL ASSETS		
Building and Improvements	48,286,039	48,205,230
Revenue Vehicles	49,218,445	46,512,808
Operations Equipment	3,290,599	3,174,316
Other Equipment	1,495,966	1,500,624
Other Vehicles	1,035,271	1,035,271
Office Equipment	<u>3,487,487</u>	<u>1,886,884</u>
	106,813,807	102,315,133
Less Accumulated Depreciation	<u>(46,307,255)</u>	<u>(42,972,894)</u>
	60,506,552	59,342,239
Construction-in-Progress	4,502,015	4,765,935
Land	<u>9,164,870</u>	<u>9,164,870</u>
Total Capital Assets	<u>74,173,437</u>	<u>73,273,044</u>
TOTAL ASSETS	<u><u>\$ 122,760,286</u></u>	<u><u>\$ 107,633,960</u></u>

The accompanying notes are an integral part of these financial statements.

SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF NET ASSETS (Continued)
JUNE 30, 2012 AND 2011

<u>LIABILITIES AND NET ASSETS</u>	<u>2012</u>	<u>2011</u>
CURRENT LIABILITIES		
Accounts Payable and Accrued Liabilities	\$ 915,561	\$ 26,987
Accrued Payroll and Employee Benefits	3,205,557	3,985,379
Deferred Rent	2,671	2,595
Workers' Compensation Liabilities	929,598	892,608
Other Accrued Liabilities	687,954	537,118
Security Deposit	16,034	16,134
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Total Current Liabilities	5,757,375	5,460,821
NON-CURRENT LIABILITIES		
Deferred Revenue - Settlement Agreement	1,336,857	1,563,383
Deferred Revenue - State Transit Authority Grant	3,610,756	1,251,229
Deferred Revenue - PTMISEA Grant	13,495,804	430,416
Deferred Revenue - Proposition 1B OHS CTSGP Grant	1,770,467	905,465
Deferred Revenue - Other	-	-
OTHER LONG-TERM LIABILITIES		
Workers' Compensation Liabilities	3,310,633	3,234,889
Other Postemployment Benefit Liabilities	10,577,195	7,387,778
	<hr/>	<hr/>
Total Liabilities	39,859,087	20,233,981
NET ASSETS		
Restricted Net Assets - PTMISEA	13,495,804	430,416
Net Assets Invested in Capital Assets	74,173,437	73,273,044
Unrestricted Net Assets	(4,768,042)	13,696,519
	<hr/>	<hr/>
Total Net Assets	82,901,199	87,399,979
	<hr/>	<hr/>
TOTAL LIABILITIES AND NET ASSETS	\$ 122,760,286	\$ 107,633,960
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The accompanying notes are an integral part of these financial statements.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF REVENUES, EXPENSES, AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
OPERATING REVENUES		
Passenger Fares	\$ 5,508,640	\$ 4,809,458
Special Transit Fares	3,264,309	3,807,181
	<u>8,772,949</u>	<u>8,616,639</u>
OPERATING EXPENSES		
Wages, Salaries, and Employee Benefits	33,255,270	31,309,520
Purchased Transportation Services	260,687	203,713
Materials and Supplies	3,178,300	3,108,165
Other Expenses	4,160,098	3,712,297
Depreciation	6,442,103	6,288,014
	<u>47,296,458</u>	<u>44,621,709</u>
Net Operating Loss	<u>(38,523,509)</u>	<u>(36,005,070)</u>
NON-OPERATING REVENUES (EXPENSES)		
Sales and Use Taxes	16,064,503	15,209,774
Transportation Development Act Assistance	5,244,964	5,001,737
Section 8/5303 Planning Fund	19,144	2,816,187
Section 9/5307 Operating Assistance	3,707,070	3,696,155
Section 18/5307 Operating Assistance	1,445,821	2,431,310
Interest Income	115,371	133,518
Rental Income	43,515	126,742
Other Revenue	475,697	242,825
Gain (Loss) on Sale and Disposal of Property, Equipment, and Inventory	<u>(31,030)</u>	<u>99,452</u>
Total Non-Operating Revenues	<u>27,085,055</u>	<u>29,757,700</u>
Net Loss Before Capital Contributions	<u>(11,438,454)</u>	<u>(6,247,370)</u>
CAPITAL CONTRIBUTIONS		
Grants Restricted for Capital Expenditures	<u>6,939,674</u>	<u>10,469,359</u>
NET ASSETS		
Increase (Decrease) in Net Assets	(4,498,780)	4,221,989
Total Net Assets, Beginning of Year	<u>87,399,979</u>	<u>83,177,990</u>
Total Net Assets, End of Year	<u>\$ 82,901,199</u>	<u>\$ 87,399,979</u>

The accompanying notes are an integral part of these financial statements.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from Customers	\$ 8,793,524	\$ 8,303,435
Payments to Employees	(33,922,358)	(31,176,155)
Payments to Suppliers	(6,422,664)	(7,675,698)
	<u>(31,551,498)</u>	<u>(30,548,418)</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:		
Operating Grants Received, Including Sales and Use Taxes	27,233,074	28,867,864
	<u>27,233,074</u>	<u>28,867,864</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from Sale of Property and Equipment	36,891	99,452
Capital Grants Received	27,506,899	9,278,054
Capital Expenditures	(7,410,417)	(10,469,359)
	<u>20,133,373</u>	<u>(1,091,853)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment and Rental Income Received	158,886	260,260
	<u>158,886</u>	<u>260,260</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	15,973,835	(2,512,147)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>26,688,958</u>	<u>29,201,105</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 42,662,793</u>	<u>\$ 26,688,958</u>
RECONCILIATION OF NET OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES		
Net Operating Loss	\$ (38,523,509)	\$ (36,005,070)
Adjustments to Reconcile Net Operating Loss to Net Cash Used in Operating Activities:		
Depreciation	6,442,103	6,288,014
Changes in Assets and Liabilities:		
(Increase) Decrease in Receivables	20,575	(313,204)
(Increase) Decrease in Inventory	85,397	(74,431)
(Increase) Decrease in Prepaid Expenses	202,550	170,741
Increase (Decrease) in Accounts Payable and Accrued Liabilities	888,574	(748,283)
Increase (Decrease) in Other Liabilities	(667,188)	133,815
	<u>(31,551,498)</u>	<u>(30,548,418)</u>
Net Cash Used in Operating Activities	<u>\$ (31,551,498)</u>	<u>\$ (30,548,418)</u>

The accompanying notes are an integral part of these financial statements.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2012 AND 2011**

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Organization

The Santa Cruz Metropolitan Transit District (Santa Cruz METRO) was formed February 9, 1969, following a favorable election in conformity with Section 9800 et. seq. of the Public Utilities Code. The transit system serves the general public in the cities of Santa Cruz, Watsonville, Scotts Valley, and Capitola and the unincorporated areas of Santa Cruz County. A Board of eleven directors and one Ex-Officio director representing the University of California, Santa Cruz governs Santa Cruz METRO. At June 30, 2012, the directors were as follows:

Chairperson:	Lynn Robinson		
Vice Chair:	Daniel Dodge		
Members:	Ellen Pirie	Margarita Alejo	Mark Stone
	Hilary Bryant	Deborah Lane	Ron Graves
	John Leopold	Dene Bustichi	Michelle Hinkle
Ex-Officio:	Donna Blitzer		

Santa Cruz METRO also serves the Highway 17 corridor into Santa Clara County to provide commuter express service through a memorandum of understanding with the California Department of Transportation, the Capitol Corridor Joint Powers Authority, and the Santa Clara Valley County Transit District (VTA). Amtrak Thruway bus service is also provided by Santa Cruz METRO on the same corridor.

B. Reporting Entity

Santa Cruz METRO and the Santa Cruz Civic Improvement Corporation (the Corporation) have a financial and operational relationship, which meets the reporting entity definition criteria of Governmental Accounting Standards Board (GASB) Statement No. 14, as amended by GASB Statement No. 39, *The Financial Reporting Entity*, for inclusion of the Corporation as a blended component unit of Santa Cruz METRO. Accordingly, the financial activities of the Corporation have been included in the basic financial statements of Santa Cruz METRO. For the years ending June 30, 2012 and 2011, these activities were minimal.

Scope of Public Service:

The Corporation is a nonprofit, public benefit corporation incorporated under the laws of the State of California and recorded by the Secretary of State in July 1986. The Corporation was formed for the sole purpose of providing financial assistance to Santa Cruz METRO for the construction and acquisition of major capital facilities.

The following are those aspects of the relationship between Santa Cruz METRO and the Corporation which satisfy GASB Statement No. 14/39 criteria.

Accountability:

1. Santa Cruz METRO's Board of Directors appointed the Corporation's Board of Directors.

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Reporting Entity (Continued)

2. Santa Cruz METRO is able to impose its will upon the Corporation based on the following:
 - All major financing arrangements, contracts, and other transactions of the Corporation must have the consent of Santa Cruz METRO.
 - Santa Cruz METRO exercises significant influence over operations of the Corporation as it is anticipated that Santa Cruz METRO will be the sole lessee of all facilities owned by the Corporation. Likewise, it is anticipated that Santa Cruz METRO's lease payments will be the sole revenue source of the Corporation.
3. The Corporation provides specific financial benefits or imposes specific financial burdens on Santa Cruz METRO based upon the following:
 - Santa Cruz METRO has assumed a “moral obligation,” and potentially a legal obligation, for any debt incurred by the Corporation.

C. Basis of Accounting and Presentation

Santa Cruz METRO is accounted for as a Business-Type Activity, as defined by GASB Statement No. 34, *Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments*, and its basic financial statements are presented on the accrual basis of accounting. Under this method, revenues are recognized when they are earned, and expenses are recognized when they are incurred.

Santa Cruz METRO adopted GASB Statement No. 34 as amended by GASB Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, as of and for the year ended June 30, 2003, and applied those standards on a retroactive basis. GASB Statement No. 34 establishes standards for external financial reporting for state and local governments and requires that resources be classified for accounting and reporting purposes into three net asset categories; namely, those invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets.

Contributed Capital/Reserved Retained Earnings:

Santa Cruz METRO receives grants from the Federal Transit Authority (FTA) and other agencies of the U.S. Department of Transportation, state, and local transportation funds for the acquisition of transit-related equipment and improvements. Prior to July 1, 2001, capital grants were recognized as donated capital to the extent that project costs under the grant had been incurred. Capital grant funds earned, less amortization equal to accumulated depreciation of the related assets, were included in contributed capital. As required by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, Santa Cruz METRO changed its method of accounting for capital grants from capital contributions to reserved non-operating revenues. In accordance with GASB Statement No. 33, capital grants are required to be included in the determination of net income resulting in an increase in net revenue of \$6,939,674 and \$10,469,359 for the fiscal years 2012 and 2011, respectively.

Under GASB Statement No. 34, contributed capital and reserved retained earnings are presented in the net asset section as net assets invested in capital assets.

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Basis of Accounting and Presentation (Continued)

Proprietary Accounting and Financial Reporting:

As required under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, Santa Cruz METRO will continue to apply all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions, and Accounting Research Bulletins (ARBs) of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements. Santa Cruz METRO has elected under GASB Statement No. 20 to not apply all FASB Statements and Interpretations issued after November 30, 1989, due to the governmental nature of Santa Cruz METRO's operations.

Net Assets:

Net assets represent the residual interest in Santa Cruz METRO's assets after liabilities are deducted. In accordance with GASB Statement No. 34, the fund equity section on the statements of net assets was combined to report total net assets and present it in three broad components: invested in capital assets, net of related debt; restricted; and unrestricted. Net assets invested in capital assets include capital assets net of accumulated depreciation. Net assets are restricted when constraints are imposed by third parties or by law through constitutional provisions or enabling legislation. All other net assets are unrestricted.

When both restricted and unrestricted resources are available for use, generally it is Santa Cruz METRO's policy to use restricted resources first, and then unrestricted resources as they are needed.

D. Cash and Cash Equivalents

Santa Cruz METRO considers all highly liquid investments with a maturity date within three months of the date acquired to be cash equivalents. Santa Cruz METRO deposits funds into an external investment pool maintained by Santa Cruz County. These deposits are considered cash equivalents. The Santa Cruz County Pooled Investment Fund is authorized to invest in obligations of the U.S. Treasury agencies and instrumentalities, commercial paper rated A-1 by Standard and Poor's Corporation or P-1 by Moody's Commercial Paper Record, bankers' acceptances, repurchase agreements, and the State Treasurer's investment pool. Cash and cash equivalents are stated at fair value. For purposes of the statements of cash flows, Santa Cruz METRO considers all highly liquid investments (including restricted assets) to be cash equivalents.

E. Inventory

Inventory is carried at cost using the first-in/first-out (FIFO) method. Inventory held by Santa Cruz METRO consists of spare bus parts and operating supplies that are consumed by Santa Cruz METRO and are not for resale purposes.

F. Restricted Assets

Certain assets are classified as restricted assets on the statements of net assets because their use is subject to externally imposed stipulations, either by laws or regulations.

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Restricted Assets (Continued)

The cash resulting from a settlement agreement, as described in Note 9, represents proceeds restricted by the FTA. The State Transit Assistance (STA) Grant, Proposition 1B Public Transportation Modernization, Improvement, and Service Enhancement Account (PTMISEA) Grant, and the Proposition 1B Office of Homeland Security (OHS) California Transit Security Grant Program (CTSGP) Grant are restricted for capital expenditures. Restricted assets at June 30 are as follows:

	<u>2012</u>	<u>2011</u>
Cash and Cash Equivalents		
Federal Transit Administration Grant	\$ 1,336,857	\$ 1,330,393
Proposition 1B PTMISEA Grant	13,495,804	430,416
Proposition 1B OHS CTSGP Grant	1,770,466	905,465
State Transit Assistance Grant	<u>818,006</u>	<u>1,251,229</u>
Total Restricted Assets	<u>\$ 17,421,133</u>	<u>\$ 3,917,503</u>

G. Property and Equipment

Property and equipment are recorded at cost. Depreciation for all such assets is computed on a straight-line basis. Estimated useful lives of assets are as follows:

Buildings and improvements	20-39 years
Revenue vehicles	12 years
Other vehicles and equipment	3-10 years

Depreciation expense on assets acquired with capital grant funds are transferred to net assets, invested in capital assets, net of related debt, after being charged to operations.

Major improvements and betterments to existing facilities and equipment are capitalized. Costs for maintenance and repairs, which do not extend the useful lives of the applicable assets, are charged to expense as incurred. Upon disposition, costs and accumulated depreciation are removed from the accounts and resulting gains or losses are included in operations.

Santa Cruz METRO completed and capitalized the Scotts Valley Transit Center in fiscal year 1999. The cost of this facility totaled \$4,063,634, which was funded by federal, state, and local funds. The Scotts Valley Redevelopment Agency (the Agency), a political subdivision of the State of California, was one of Santa Cruz METRO's funding sources for this project and has retained an interest in the property. The title to the property is retained by both Santa Cruz METRO and the Agency as tenants in common with each party holding an individual interest in proportion to each party's financial participation in the project. The Agency's portion of the property is 13.87%. The Agency's portion is not recorded in Santa Cruz METRO's basic financial statements.

H. Sales and Use Tax

Santa Cruz METRO receives a 0.5% sales and use tax levied on all taxable sales in Santa Cruz County, which is collected and administered by the California State Board of Equalization. Additionally, Santa Cruz METRO is allocated, through the Santa Cruz County Regional Transportation Commission, a portion of the 0.25% sales and use tax levied by the Transportation Development Act (TDA).

I. Operating Assistance Grants

Operating assistance grants are recognized as revenue in the grant period earned.

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

J. Self-Insurance

Santa Cruz METRO is self-insured for the first \$250,000 of general and vehicular liability. For settlements in excess of \$250,000, Santa Cruz METRO has total coverage up to \$20,000,000 per occurrence. Additionally, Santa Cruz METRO is self-insured up to \$350,000 for workers' compensation claims. Santa Cruz METRO has recorded a liability for estimated claims to be paid including incurred but not reported claims.

K. Employee Benefits

Annual and medical leave benefits are accrued when earned and reduced when used. Any paid medical leave accrued beyond 96 hours may, at the employee's option, be converted to annual leave and credited to the employee's annual leave schedule or paid in cash, depending on the bargaining unit, at 100% of the earned rate. Employees are paid accrued and unused annual leave at the time of separation from Santa Cruz METRO service.

L. Payroll

Santa Cruz METRO contracts with the Santa Cruz County Auditor-Controller to provide payroll processing services.

M. Pension Costs

Pension costs are expensed as incurred. These costs equal the actuarially determined annual contribution amount.

N. 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

O. Reclassifications

Certain reclassifications have been made to prior period amounts to conform to the classifications used in the current period. Such reclassifications had no effect on Santa Cruz METRO's financial positions or results of operations for the periods presented.

P. Future Governmental Accounting Standards Board Statements

GASB Statement No. 60 – *Accounting and Financial Reporting for Service Concession Arrangements* addresses accounting and financial reporting issues related to public - private and public - public partnerships. The statement is effective for periods beginning after December 15, 2011. Management has not evaluated the effect of GASB Statement No. 60 on the Santa Cruz METRO financial statements.

GASB Statement No. 61 – *The Financial Reporting Entity: Omnibus, an Amendment of GASB Statements No. 14 and No. 34* modifies a number of provisions with regard to reporting of component units within a financial reporting entity. The statement is effective for periods beginning after June 15, 2012. Santa Cruz METRO has elected to not early implement GASB Statement No. 61 and has not determined its effect on the Santa Cruz METRO financial statements.

NOTE 1 – OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

P. Future Governmental Accounting Standards Board Statements (Continued)

GASB Statement No. 62 – *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements – FASB Statements and Interpretations, APB Opinions, and ARBs of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. The statement is effective for periods beginning after December 15, 2011. However, as the statement codifies what is in current practice, there is no net effect on Santa Cruz METRO's accounting or financial reporting upon the statement's implementation.

GASB Statement No. 63 – *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* modifies current financial reporting of those elements. The largest change will be the replacement of the current Statement of Net Plan Assets with a Statement of Net Plan Position upon implementation for periods beginning after December 15, 2011. GASB Statement No. 63 will not have an effect on Santa Cruz METRO's financial statements.

GASB Statement No. 64 – *Derivative Instruments: Application of Hedge Accounting Termination Provisions* amends current accounting and financial reporting related to terminations of swap agreements due to default or other termination events. In certain instances where swap counterparties or credit support providers are replaced, hedge accounting may continue, rather than cease. The provisions of GASB Statement No. 64 are effective for financial statements beginning after June 15, 2011. Because Santa Cruz METRO does not enter into hedge agreements with swap providers for the purpose of managing risk beyond investment return, GASB Statement No. 64 will not apply.

GASB Statement No. 65 – *Items Previously Reported as Assets and Liabilities* establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2012. Santa Cruz METRO has not determined the effects of the implementation of this statement on its financial statements.

GASB Statement No. 66 – *Technical Corrections—2012—an Amendment of GASB Statements No. 10 and No. 62* is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2012. Santa Cruz METRO does not expect the implementation of this statement to have a material effect on the financial statements.

GASB Statement No. 67 – *Financial Reporting for Pension Plans—an Amendment of GASB Statement No. 25* improves financial reporting by state and local governmental pension plans. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2013. Santa Cruz METRO has not determined the effects of the implementation of this statement on its financial statements.

GASB Statement No. 68 – *Accounting and Financial Reporting for Pensions—an Amendment of GASB Statement No. 27* improves accounting and financial reporting by state and local governments for pensions. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2014. The implementation of this standard will have a material effect on the Santa Cruz METRO financial statements.

NOTE 2 – CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Cash on Hand	\$ 55,158	\$ 46,718
Demand Deposits	590,291	480,887
Deposits in Santa Cruz County Pooled Investment Fund	<u>42,017,344</u>	<u>26,161,353</u>
	<u>\$ 42,662,793</u>	<u>\$ 26,688,958</u>

Cash on Hand and Cash in Banks

Investments Authorized by the California Government Code and Santa Cruz METRO's Investment Policy

The table below identifies the **investment types** that are authorized for Santa Cruz METRO by the California Government Code (or Santa Cruz METRO's investment policy, where more restrictive). The table also identifies certain provisions of the California Government Code (or Santa Cruz METRO's investment policy, where more restrictive) that address **interest rate risk**, **credit risk**, and **concentration of credit risk**.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
Bankers' Acceptances	180 days	None	None
Commercial Paper	270 days	None	None
Negotiable Certificates of Deposit	5 years	None	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	None	None
Medium-Term Notes	5 years	None	None
Mutual Funds	N/A	None	None
Money Market Mutual Funds	N/A	None	None
Mortgage Pass-Through Securities	5 years	None	None
County Pooled Investment Funds	N/A	100%	None
Local Agency Investment Fund (LAIF)	N/A	None	None

Disclosures 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.

Information about the sensitivity of the fair values of Santa Cruz METRO's investments to market interest rate fluctuations is provided by the following table that shows the distribution of Santa Cruz METRO's investments by maturity:

<u>Investment Type</u>	<u>Amount</u>	<u>Remaining Maturity (in Months)</u>			
		<u>12 Months or Less</u>	<u>13 to 24 Months</u>	<u>25 to 60 Months</u>	<u>More Than 60 Months</u>
County Pooled Investment Fund	<u>\$ 42,017,344</u>	<u>\$ 42,017,344</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

NOTE 2 – CASH AND CASH EQUIVALENTS (Continued)

Cash on Hand and Cash in Banks (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 (where applicable) the California Government Code, Santa Cruz METRO's investment policy, and the actual rating as of year-end for each investment type. The column marked "exempt from disclosure" identifies those investment types for which GASB Statement No. 40 does not require disclosure as to credit risk:

Investment Type	Amount	Minimum Legal Rating	Exempt From Disclosure	Rating as of Year-End		
				AAA	Aa	Not Rated
County Pooled Investment Fund	<u>\$42,017,344</u>	<u>N/A</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$42,017,344</u>

Concentration of Credit Risk

The investment policy of Santa Cruz METRO contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. Santa Cruz METRO did not have any investments in any one issuer (other than external investment pools) that represent 5% or more of total Santa Cruz METRO's investments at June 30, 2012 or 2011.

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 (e.g., broker-dealer) 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 Santa Cruz METRO's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). 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.

Custodial Credit Risk

GASB Statement No. 40 requires that the following disclosure be made with respect to custodial credit risks relating to deposits and investments: None of Santa Cruz METRO's deposits with financial institutions in excess of federal depository insurance limits were held in uncollateralized accounts.

Investment in Santa Cruz County Pooled Investment Fund

Santa Cruz METRO is a voluntary participant in the Santa Cruz County Pooled Investment Fund. The fair value of Santa Cruz METRO's investment in this pool is reported in the accompanying basic financial statements at amounts based upon Santa Cruz METRO's pro-rata share of the fair value provided by the Santa Cruz County for the entire Santa Cruz County portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by the Santa Cruz County, which are recorded on an amortized cost basis.

NOTE 3 – RECEIVABLES

Receivables at June 30 are as follows:

	<u>2012</u>	<u>2011</u>
Federal Grants	\$ 23,260	\$ 42,610
State Grants	1,731,162	3,026,054
Local Grants	-	176
Sales Tax Revenue	2,644,200	2,506,200
Other	692,918	976,455
	<u>\$ 5,091,540</u>	<u>\$ 6,551,495</u>

NOTE 4 – CHANGES IN CAPITAL ASSETS

Facilities, property, and equipment at June 30 are summarized as follows:

June 30, 2012

	<u>Balance July 1, 2011</u>	<u>Additions and Transfers</u>	<u>Retirements and Transfers</u>	<u>Balance June 30, 2012</u>
Non-Depreciated Assets				
Land	\$ 9,164,870	\$ -	\$ -	\$ 9,164,870
Construction-in-Progress	4,765,935	7,410,417	(7,674,337)	4,502,015
Total Non-Depreciated Assets	13,930,805	7,410,417	(7,674,337)	13,666,885
Depreciated Assets				
Building and Improvements	48,205,230	190,725	(109,916)	48,286,039
Revenue Vehicles	46,512,808	5,626,839	(2,921,202)	49,218,445
Operations Equipment	3,174,316	239,075	(122,792)	3,290,599
Other Equipment	1,500,624	-	(4,658)	1,495,966
Other Vehicles	1,035,271	-	-	1,035,271
Office Equipment	1,886,884	1,617,698	(17,095)	3,487,487
Total Depreciated Assets	102,315,133	7,674,337	(3,175,663)	106,813,807
Less Accumulated Depreciation	<u>(42,972,894)</u>	<u>(6,442,103)</u>	<u>3,107,742</u>	<u>(46,307,255)</u>
Depreciated Assets Net of Accumulated Depreciation	<u>59,342,239</u>	<u>1,232,234</u>	<u>(67,921)</u>	<u>60,506,552</u>
Total Capital Assets	<u>\$ 73,273,044</u>	<u>\$ 8,642,651</u>	<u>\$ (7,742,258)</u>	<u>\$ 74,173,437</u>

Depreciation expense at June 30, 2012, was \$6,442,103.

NOTE 4 – CHANGES IN CAPITAL ASSETS (Continued)

June 30, 2011

	Balance July 1, 2010	Additions and Transfers	Retirements and Transfers	Balance June 30, 2011
Non-Depreciated Assets				
Land	\$ 9,164,870	\$ -	\$ -	\$ 9,164,870
Construction-in-Progress	36,681,106	3,340,193	(35,255,364)	4,765,935
Total Non-Depreciated Assets	45,845,976	3,340,193	(35,255,364)	13,930,805
Depreciated Assets				
Building and Improvements	12,483,953	35,721,942	(665)	48,205,230
Revenue Vehicles	44,599,626	4,034,227	(2,121,045)	46,512,808
Operations Equipment	1,810,861	2,138,658	(775,203)	3,174,316
Other Equipment	1,500,624	-	-	1,500,624
Other Vehicles	1,169,471	-	(134,200)	1,035,271
Office Equipment	1,453,135	489,703	(55,954)	1,886,884
Total Depreciated Assets	63,017,670	42,384,530	(3,087,067)	102,315,133
Less Accumulated Depreciation	(39,771,947)	(6,288,014)	3,087,067	(42,972,894)
Depreciated Assets Net of Accumulated Depreciation	23,245,723	36,096,516	-	59,342,239
Total Capital Assets	<u>\$ 69,091,699</u>	<u>\$ 39,436,709</u>	<u>\$ (35,255,364)</u>	<u>\$ 73,273,044</u>

Depreciation expense at June 30, 2011, was \$6,288,014.

NOTE 5 – CAPITAL GRANTS

Santa Cruz METRO receives grants from the Federal Transit Authority (FTA), which provides financing for the acquisition of rolling stock and construction of facilities. Santa Cruz METRO also receives grants under the State TDA primarily for the acquisition of rolling stock and support equipment, and purchase of furniture and fixtures.

A summary of federal, state, and local grant activity for the years ended June 30 is as follows:

	2012	2011
Federal Grants	\$ 5,541,880	\$ 5,691,481
State Grants	1,397,794	4,777,878
Total Capital Grants	<u>\$ 6,939,674</u>	<u>\$ 10,469,359</u>

NOTE 6 – COMMITMENTS

Santa Cruz METRO leases a number of its facilities under operating leases through 2016. For the years ended June 30, 2012 and 2011, rental expense relating to the leases was \$212,684 and \$284,454, respectively. In addition, Santa Cruz METRO receives rent income from retail space in its transit centers. Minimum net lease payments and receipts for existing operating leases are as follows:

<u>Year Ending June 30</u>	<u>Lease Commitments</u>	<u>Rental Income</u>	<u>Net</u>
2013	\$ 214,124	\$ 133,619	\$ 80,505
2014	174,211	125,924	48,287
2015	21,949	128,268	(106,319)
2016	22,388	64,387	(41,999)
Thereafter	-	14,316	(14,316)
	<u>\$ 432,672</u>	<u>\$ 466,514</u>	<u>\$ (33,842)</u>

NOTE 7 – JOINT VENTURES (JOINT POWERS AUTHORITY WITH CalTIP)

Santa Cruz METRO participates in a joint powers authority (JPA), the California Transit Insurance Pool (CalTIP). The relationship between Santa Cruz METRO and the JPA is such that the JPA is not a component unit of Santa Cruz METRO for financial reporting purposes.

CalTIP arranges for and provides property and liability insurance for its 34 members. CalTIP is governed by a board that controls the operations of CalTIP, including selection of management and approval of operating budgets, independent of any influence by the member districts. Each member district pays a premium commensurate with the level of coverage requested and shares in surpluses and deficits proportionate to their participation in CalTIP.

Condensed audited financial information of CalTIP for the years ended April 30 (most recent information available) is as follows:

	<u>2012</u>	<u>2011</u>
Total Assets	\$ 27,464,131	\$ 26,331,874
Total Liabilities	<u>13,027,097</u>	<u>11,049,263</u>
Fund Balance	<u>\$ 14,437,034</u>	<u>\$ 15,282,611</u>
Total Revenues	\$ 5,284,303	\$ 5,304,038
Total Expenditures	<u>6,129,880</u>	<u>6,569,449</u>
Net Decrease in Fund Balance	<u>\$ (845,577)</u>	<u>\$ (1,265,411)</u>

CalTIP has not calculated Santa Cruz METRO's share of year-end assets, liabilities, or fund balance.

NOTE 8 – WATSONVILLE FLEET MAINTENANCE FACILITY SETTLEMENT RECEIPT

Santa Cruz METRO's fleet maintenance facility in Watsonville was damaged in the Loma Prieta earthquake (the earthquake) in October 1989. An engineering study concluded that the demolition of the existing facility and construction of a new facility was the most practical course of action. Therefore, the net book value of the facility was written off the books in a prior year.

NOTE 8 – WATSONVILLE FLEET MAINTENANCE FACILITY SETTLEMENT RECEIPT (Continued)

In addition, due to design and construction deficiencies by the design and building contractors involved in the original project, Santa Cruz METRO initiated litigation against the contractors and came to a settlement agreement with said contractors on May 30, 1995. In accordance with this agreement, the contractors remitted \$4,776,858 (including \$171,538 in costs) to Santa Cruz METRO during fiscal year 1996, representing damages less attorney fees. FTA Section 3/5309 restricts the use of these proceeds, and the interest earned thereon. Accordingly, the net restricted amount of \$1,336,857 and \$1,330,393 is reflected on the statements of net assets as deferred revenue at June 30, 2012 and 2011, respectively.

NOTE 9 – CONTINGENCIES

Santa Cruz METRO has received state and federal funds for specific purposes that are subject to review and audit by grantor agencies. Although such audits could generate expenditure disallowances under terms of the grants, Santa Cruz METRO believes that any required reimbursement will not be material.

Additionally, Santa Cruz METRO is party to various claims and litigation in the normal course of business. In the opinion of management and in-house counsel, any ultimate losses have been adequately provided for in the basic financial statements.

NOTE 10 – DEFINED BENEFIT PENSION PLAN

Plan Description

Santa Cruz METRO's defined benefit pension plan, the Miscellaneous Plan for Santa Cruz Metropolitan Transit District (the Plan), provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The Plan is part of the Public Agency portion of the California Public Employees' Retirement System (CalPERS), an agent multiple-employer plan administered by CalPERS, which acts as a common investment and administrative agent for participating public employers with the State of California. A menu of benefit provisions as well as other requirements is established by state statutes within the Public Employees' Retirement Law. Santa Cruz METRO selects optional benefit provisions from the benefit menu by contract with CalPERS and adopts those benefits through Board of Directors action. CalPERS issues a separate comprehensive annual financial report. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95814.

Funding Policy

There are 292 active plan members in the Plan as of June 30, 2012, which are required to contribute a percentage of their annual covered salary. In lieu of salary increases and for employees who agreed to salary reductions in certain prior years, Santa Cruz METRO agreed to pay a portion of the employee contribution, based on formulas negotiated in their labor agreements. Santa Cruz METRO is also required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the fiscal year ended June 30, 2012, was 17.205%. The contribution requirements of the Plan members are established by state statute and the employer contribution rate is established and may be amended by CalPERS.

NOTE 10 – DEFINED BENEFIT PENSION PLAN (Continued)Annual Pension Cost

For the fiscal year ended June 30, 2012, Santa Cruz METRO's annual pension cost of \$2,664,532 was equal to Santa Cruz METRO's required and actual contributions. This includes Santa Cruz METRO's contribution to the employee contribution requirement. The required contribution for the fiscal year ended June 30, 2012, was determined as part of the June 30, 2009, actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 7.75% investment rate of return (net of administration expenses), (b) projected salary increases that vary by duration of service ranging from 3.55% to 14.45% for miscellaneous members, and (c) 3.25% cost-of-living adjustment. Both (a) and (b) include an inflation component of 3.0%. The actuarial value of the Plan's assets was determined using a technique that smoothes the effect of short-term volatility in the market value of investments over a three-year period. The Plan's unfunded actuarial accrued liability (UAAL) is being amortized as a level percentage of projected payroll on a closed basis.

Three-Year Trend Information for the Plan

Three-year trend information, with respect to Santa Cruz METRO's participation in CalPERS, is as follows:

<u>Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/2010	\$ 2,151,927	100%	\$ -
6/30/2011	\$ 2,156,777	100%	\$ -
6/30/2012	\$ 2,664,532	100%	\$ -

The funded status for the prior three years to June 30, 2010, (the last available date) for Santa Cruz METRO is as follows:

<u>Valuation Date</u>	<u>Entry Age Actuarial Accrued Liability</u>	<u>Actuarial Value of Assets</u>	<u>Unfunded/ (Overfunded) Liability</u>	<u>Funded Ratio</u>	<u>Annual Covered Payroll</u>	<u>UAAL as a % of Payroll</u>
6/30/2008	\$ 97,329,553	\$ 85,056,437	\$ 12,273,116	87.4%	\$ 16,065,532	76.4%
6/30/2009	\$ 109,418,745	\$ 89,621,182	\$ 19,797,563	81.9%	\$ 16,397,024	120.7%
6/30/2010	\$ 115,194,294	\$ 93,813,512	\$ 21,380,782	81.4%	\$ 16,109,672	132.7%

NOTE 11 – DEFERRED COMPENSATION PLAN

Santa Cruz METRO offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 and provisions of the Government Code of the State of California. The plan, available to all Santa Cruz METRO employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, or unforeseeable emergency. Santa Cruz METRO employees participate in two such plans, the Great-West Life and Annuity Insurance (Great-West) plan and the other through CalPERS.

At June 30, 2012 and 2011, all amounts held under the Great-West plan and the CalPERS plan are held in trust and are not reflected on the accompanying statement of net assets as required under GASB Statement No. 27, *Accounting Standards for Pensions by State and Local Governmental Employers*.

Complete financial statements for Great-West can be obtained from Great-West at PO Box 173764 Denver, CO 80217-3764. Complete financial statements for CalPERS can be obtained from CalPERS at Lincoln Plaza North, 400 Q Street, Sacramento, CA 94229.

NOTE 12 – RISK MANAGEMENT

Santa Cruz METRO is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters for which Santa Cruz METRO carries commercial insurance. Santa Cruz METRO has established limited risk management programs for workers' compensation, and general and vehicular liability, as described in Note 1, as well.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNR). The IBNR for workers' compensation was based on an actuarial study dated May 2010. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. Changes in the balances of claims liabilities are as follows:

	<u>2012</u>	<u>2011</u>
Workers' Compensation Liabilities:		
Unpaid Claims, Beginning of Fiscal Year	\$ 4,127,497	\$ 4,083,077
Incurred Claims (Including IBNRs)	(1,085,912)	(953,272)
Claim Payments	<u>1,198,646</u>	<u>997,692</u>
Unpaid Claims, End of Fiscal Year	<u>\$ 4,240,231</u>	<u>\$ 4,127,497</u>

NOTE 13 – TRANSPORTATION DEVELOPMENT ACT/CALIFORNIA ADMINISTRATIVE CODE

Santa Cruz METRO is subject to compliance with the TDA provisions, Sections 6634 and 6637 of the California Administrative Code and Sections 99267, 99268.1, and 99314.6 of the Public Utilities Code.

Section 6634

Pursuant to Section 6634, a transit claimant is precluded from receiving monies from the Local Transportation Fund and the STA Fund in an amount which exceeds the claimant's capital and operating costs, less the required fares, and local support. Santa Cruz METRO did not receive TDA or State Transit Assistance revenues in excess of the prescribed formula amounts.

Section 6637

Pursuant to Section 6637, a claimant must maintain its accounts and records in accordance with the Uniform System of Accounts and Records for Transit Operators adopted by the State Controller. Santa Cruz METRO did maintain its accounts and records in accordance with the Uniform System of Accounts and Records for Transit Operators.

Sections 99267, 99268.1, and 99314.6

Pursuant to the TDA, Santa Cruz METRO is defined as an older operator and is not required to meet the fare box ratio requirement of the TDA. Santa Cruz METRO has met the 50% expenditure limitation requirement.

NOTE 14 – PUBLIC TRANSPORTATION MODERNIZATION, IMPROVEMENT, AND SERVICE ENHANCEMENT ACCOUNT (PTMISEA)

In November 2006, California voters passed a bond measure enacting the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, Proposition 1B. Of the \$19.925 billion of State general obligation bonds authorized, \$4 billion was set aside by the State, as instructed by the statute, as the Public Transportation Modernization, Improvement, and Service Enhancement Account (PTMISEA). These funds are available to the California Department of Transportation for intercity rail projects and to transit operators in California for rehabilitation, safety, or modernization improvements; capital service enhancements or expansions; new capital projects; bus rapid transit improvements; or for rolling stock procurement, rehabilitation, or replacement.

The audit of public transportation operator finances, pursuant to Section 99245 of the Public Utilities Code (PUC) and required under the TDA, was expanded to include verification of receipt and appropriate expenditure of PTMISEA bond funds.

The Santa Cruz County Regional Transportation Commission (SCCRTC) is responsible for allocating the Proposition 1B PUC Section 99313 funds in Santa Cruz County. In December 2007, the SCCRTC programmed 100% of its share of Section 99313 Proposition 1B PTMISEA funds (approximately \$2.1 million) to Santa Cruz METRO for the Consolidated MetroBase Project. Funds audited include the SCCRTC share of PUC Section 99313 Proposition 1B transit funds that have been passed-through to Santa Cruz METRO.

During the fiscal year ended June 30, 2012, Santa Cruz METRO applied for and received proceeds of \$13,501,970 and earned interest of \$26,866 from the State's PTMISEA account for construction funding for the Consolidated MetroBase Project. During the fiscal year ended June 30, 2012, qualifying expenditures of \$463,448 were incurred and the remaining balance of \$13,495,804 including accrued interest was deferred. Qualifying expenditures must be encumbered within three years from the date of the allocation and expended within three years from the date of encumbrance.

**Schedule of PTMISEA Bond 1B Grants
For the Year Ended June 30, 2012**

	<u>2012</u>
Balance - beginning of the year	\$ 430,416
Receipts:	
Warrant No 66-301674 - Deposited 10/27/11	2,491,923
Warrant No 66-830063 - Deposited 2/13/12	11,010,047
Interest accrued 7/1/2011 through 6/30/2012	26,866
Expenses:	
MetroBase Construction	<u>(463,448)</u>
Balance - end of year	<u>\$ 13,495,804</u>

NOTE 14 – PUBLIC TRANSPORTATION MODERNIZATION, IMPROVEMENT, AND SERVICE ENHANCEMENT ACCOUNT (PTMISEA) (Continued)

**Schedule of PTMISEA Bond 1B Grants
For the Year Ended June 30, 2011**

	<u>2011</u>
Balance - beginning of the year	\$ 1,475,663
Receipts:	
Interest accrued 7/1/2010 through 6/30/2011	5,091
Expenses:	
MetroBase Construction	<u>(1,050,338)</u>
Balance - end of year	<u>\$ 430,416</u>

NOTE 15 – POSTEMPLOYMENT BENEFITS OTHER THAN PENSION BENEFITS

Plan Description

Santa Cruz METRO provides post-retirement CalPERS medical benefits to qualified retired employees age 50 and older (including eligible dependents) who have completed at least five years of CalPERS eligible service. Santa Cruz METRO pays medical premiums depending on bargaining union contract requirements. If the retiree has ten years of Santa Cruz METRO eligible service, Santa Cruz METRO provides post-retirement dental and vision benefits for qualified retirees (including eligible dependents), and life insurance for the retiree only, until the retiree reaches age 65. Bus operators who retired and reached the age of 65 prior to June 30, 1994, will continue to receive dental and vision coverage beyond age 65. Life insurance is not provided to management retirees who retired prior to July 1, 2005. The costs of providing these benefits are recognized when paid. Santa Cruz METRO has recognized approximately \$2,324,583 and \$2,023,718 of expense for these benefits for the years ending June 30, 2012 and 2011, respectively.

Annual OPEB Cost and Net OPEB Obligation

Santa Cruz METRO's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. For fiscal year 2011-12, Santa Cruz METRO's annual OPEB cost was \$5,514,000. Santa Cruz METRO's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the year ended June 30, 2012, were as follows:

Annual required contribution	\$ 5,567,000
Interest on net OPEB obligation	280,000
Adjustments to annual required contribution	<u>(333,000)</u>
Annual OPEB cost	5,514,000
Contributions made	<u>2,324,583</u>
Change in net OPEB obligation (asset)	3,189,417
Net OPEB obligation (asset) - beginning of year	<u>7,387,778</u>
Net OPEB obligation (asset) - end of year	<u>\$ 10,577,195</u>

NOTE 15 – POSTEMPLOYMENT BENEFITS OTHER THAN PENSION BENEFITS (Continued)Annual OPEB Cost and Net OPEB Obligation (Continued)

Year Ended June 30,	Annual OPEB Cost	Actual Employer Contributions	Percentage of Annual OPEB Cost Contributed	Net Ending OPEB Obligation (Asset)
6/30/2010	\$ 4,154,630	\$ 1,597,810	38.46%	\$ 5,118,074
6/30/2011	\$ 4,293,422	\$ 2,023,718	47.14%	\$ 7,387,778
6/30/2012	\$ 5,514,000	\$ 2,324,583	42.16%	\$ 10,577,195

Funding Policy, Funded Status, and Funding Progress

Santa Cruz METRO's required contribution is based on pay-as-you-go financing requirements. For fiscal year 2011-12, Santa Cruz METRO contributed \$2,324,583 to the plan.

As of June 30, 2011, the most recent actuarial valuation date, the actuarial accrued liability (AAL) for benefits was \$59,164,000, all of which was unfunded.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and probability about the occurrence of future events far into the future. Amounts determined regarding the funded status of a plan and the annual required contributions of Santa Cruz METRO are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

The schedule of funding progress, presented as required supplementary information following the notes to the basic financial statements, will present multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Calculations of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with long-term perspective of the calculations.

The actuarial assumptions used for rates of employee turnover, retirement, and mortality, as well as economic assumptions regarding healthcare inflation and interest were based on a standard set of actuarial assumptions modified as appropriate for Santa Cruz METRO. Turnover, mortality and retirement rates were taken from the CalPERS actuarial table for miscellaneous employees, which closely matches Santa Cruz METRO experience. Healthcare inflation rates are based on the general health care environment. Actual healthcare premiums through 2013 were used and then projected to increase in future years by 8.5% (8.9% for Medicare eligible premiums) in 2014, with the increases gradually declining until reaching 5% in 2021 (5% future premiums increases assumed for all years after 2012). The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on a closed basis over 30 years from June 30, 2008, with 26 years remaining as of June 30, 2012.

NOTE 16 – SUBSEQUENT EVENTS

In September 2012, Santa Cruz METRO entered in to a contract with TRC Solutions, Inc., for construction management services for the Judy K. Souza Operations Facility component of the MetroBase Project in an amount not to exceed \$1,495,440.

NOTE 16 – SUBSEQUENT EVENTS (Continued)

In December 2012, Santa Cruz METRO entered into a contract with Lewis C. Nelson and Sons, Inc., in the amount of \$13,572,000 for the construction of the Judy K. Souza Operations Facility.

Subsequent events were evaluated by management through December 20, 2012, which is the date of issuance.

REQUIRED SUPPLEMENTARY INFORMATION

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF FUNDING PROGRESS
DEFINED BENEFIT PENSION PLAN
JUNE 30, 2012**

Supplementary information is intended to show the progress made towards funding benefit obligations. Required three-year supplemental information, available to date, for Santa Cruz METRO is as follows:

Valuation Date	Entry Age Actuarial Accrued Liability	Actuarial Value of Assets	Unfunded/ (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	UAAL as a % of Payroll
6/30/2008	\$ 97,329,553	\$ 85,056,437	\$ 12,273,116	87.4%	\$ 16,065,532	76.4%
6/30/2009	\$ 109,418,745	\$ 89,621,182	\$ 19,797,563	81.9%	\$ 16,397,024	120.7%
6/30/2010	\$ 115,194,294	\$ 93,813,512	\$ 21,380,782	81.4%	\$ 16,109,672	132.7%

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF FUNDING PROGRESS
OTHER POSTEMPLOYMENT BENEFITS
JUNE 30, 2012**

Supplementary information is intended to show the progress made towards funding benefit obligations. Required three-year supplemental information, available to date, for Santa Cruz METRO is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b - a)/c]
4/1/2008	\$ -	\$ 44,208,804	\$ 44,208,804	0.00%	\$ 16,065,532	275.18%
4/1/2010	\$ -	\$ 43,442,791	\$ 43,442,791	0.00%	\$ 16,109,672	269.67%
6/30/2011	\$ -	\$ 59,164,000	\$ 59,164,000	0.00%	\$ 15,925,000	371.52%

SUPPLEMENTARY INFORMATION

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF OPERATING EXPENSES
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011**

	2012	2011
Labor		
Operators' salaries and wages	\$ 7,124,710	\$ 7,333,267
Other salaries and wages	6,242,010	6,299,332
Overtime	1,997,538	1,983,559
	15,364,258	15,616,158
Fringe Benefits		
Absence with pay	2,951,594	3,074,137
Pension plans	2,664,532	2,156,777
Vision, medical, and dental plans	7,268,173	6,575,549
Workers' compensation insurance	1,311,380	1,042,111
Disability insurance	307,265	374,226
Other fringe benefits	198,651	200,858
Other postemployment benefits	3,189,417	2,269,704
	17,891,012	15,693,362
Services		
Accounting	77,560	74,742
Administrative and banking	275,529	224,273
Professional and technical services	496,404	411,457
Security	324,827	370,312
Outside repairs	817,411	951,714
Other services	140,309	136,524
	2,132,040	2,169,022
Materials and Supplies Consumed		
Fuels and lubricants	2,051,549	2,145,437
Tires and tubes	139,709	210,370
Vehicle parts	672,431	525,453
Other materials and supplies	314,611	226,905
	3,178,300	3,108,165
Utilities	472,076	472,499
Casualty and Liability Costs	1,096,512	572,416
Taxes and Licenses	41,987	45,873
Purchased Transportation Services		
Paratransit	260,687	203,713
Miscellaneous Expenses	185,703	154,670
Equipment and Facility Lease	231,780	297,817
Depreciation		
Property acquired with operator funds	288,640	390,392
Property acquired by federal, state, or TDA funds	6,153,463	5,897,622
	6,442,103	6,288,014
Total Operating Expenses	\$ 47,296,458	\$ 44,621,709

OTHER SCHEDULES AND REPORTS

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2012**

<u>Federal Grantor / Program Title</u>	<u>Federal CFDA No.</u>	<u>Pass-Through Grantor's Number</u>	<u>Total Federal Expenditures</u>
U.S. DEPARTMENT OF TRANSPORTATION			
Direct Programs:			
Federal Transit Administration (FTA)			
Cluster Defined by the Department of Transportation			
Section 3/5309 Consolidation			
SGR - CNG Bus Purchase	20.500*	CA-04-0185	\$ 4,771,973
Pacific Station - ROW Acquisition	20.500*	CA-03-0730	<u>11,612</u>
			<u>4,783,585</u>
Section 9/5307			
Operating Assistance	20.507*	CA-90-Y907	4,727,487
ARRA - PC Vans, Fareboxes, IT Equip	20.507*	CA-96-X030	<u>519,218</u>
			<u>5,246,705</u>
Other Programs			
Section 18/5311-5317			
Rural Operating Assistance - 5311	20.509	641166	156,312
Section 18/5304			
AMBAG Watsonville Transit Planning Study	20.515	WE 672	11,512
On-Board Transit Ridership Survey-CT Sub-award	20.515	N/A	<u>7,632</u>
			<u>19,144</u>
Total Expenditures of Federal Awards			<u><u>\$ 10,205,746</u></u>

* Major federal financial assistance program.

See accompanying notes to schedule of expenditures of federal awards.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2012**

NOTE 1 – GENERAL

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the Santa Cruz Metropolitan Transit District (Santa Cruz METRO). Federal financial assistance received directly from federal agencies, as well as federal financial assistance passed through other governmental agents, is included on the schedule.

NOTE 2 – BASIS OF ACCOUNTING

The accompanying Schedule of Expenditures of Federal Awards has been prepared on the accrual basis of accounting. Federal capital grant funds are used to purchase property, plant, and equipment. Federal grants receivable are included in capital and operating grants receivable, which also includes receivables from state and local grant sources.

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SUPPLEMENTAL REVENUE, EXPENSES, AND PERFORMANCE REPORT
(BASED ON FEDERAL TRANSIT AUTHORITY (FTA) ACCOUNT GROUPING GUIDELINES)**

	2012	2011	2010	2012 to 2011 % Change	2011 to 2010 % Change
Revenues					
Passenger Fares	\$ 8,772,949	\$ 8,616,639	\$ 8,427,944	1.8%	2.2%
Sales and Use Tax ⁽¹⁾	16,064,503	15,209,774	14,320,288	5.6%	6.2%
Non-Operating Revenues	586,628	602,537	569,113	-2.6%	5.9%
TDA	5,244,964	5,001,737	5,001,737	4.9%	0.0%
Federal Operating Assistance ⁽²⁾	5,257,104	8,943,652	4,436,651	-41.2%	101.6%
Total Revenues	\$ 35,926,148	\$ 38,374,339	\$ 32,755,733	-6.4%	17.2%
Expenses					
Route Operation	24,399,195	\$ 25,095,284	\$ 25,013,598	-2.8%	0.3%
Vehicle Maintenance	5,130,727	4,939,279	5,084,431	3.9%	-2.9%
Facilities Maintenance	1,886,947	1,884,113	1,835,936	0.2%	2.6%
General Administration ⁽³⁾	9,437,482	6,415,019	5,810,294	47.1%	10.4%
Total Expenses (excluding depreciation)	\$ 40,854,351	\$ 38,333,695	\$ 37,744,259	6.6%	1.6%
Performance Indicators					
Total Passengers ⁽⁴⁾	5,463,380	5,871,671	5,934,035	-7.0%	-1.1%
Revenue Hours	273,212	282,775	282,381	-3.4%	0.1%
Revenue Miles	3,919,424	4,121,744	4,259,386	-4.9%	-3.2%
Farebox Recovery Ratio ⁽⁵⁾	21.5%	22.5%	22.3%	-4.4%	0.9%
Cost/Passenger ⁽⁶⁾	\$ 7.48	\$ 6.53	\$ 6.36	14.5%	2.7%
Cost/Hour ⁽⁷⁾	\$ 149.53	\$ 135.56	\$ 133.66	10.3%	1.4%
Cost/Mile ⁽⁸⁾	\$ 10.42	\$ 9.30	\$ 8.86	12.0%	5.0%
Full Time Equivalent Employees	292	281	303	3.9%	-7.3%
Active Fleet - Fixed Route ⁽⁹⁾	120	110	112	9.1%	-1.8%
Active Fleet - Paratransit	47	45	37	4.4%	21.6%

⁽¹⁾ Sales and Use Tax Revenues have increased from prior year due to increased consumer spending as a result of increased consumer confidence and an improving economy.

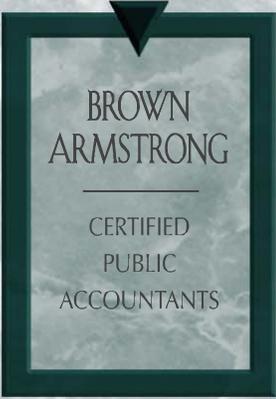
⁽²⁾ Federal Operating Assistance decreased in fiscal year 2012 due to a change in allocation of STA funds from the operating budget to the capital budget to fund the Judy K. Souza Operations Facility and the expiration of the Alternative Fuel Tax Rebate program in December 2011.

⁽³⁾ General Administration expenses increased primarily due to the treatment of the Governmental Accounting Standards Board (GASB) Statement No. 45 Other Postemployment Benefits (OPEB) annual liability entry coupled with increased medical and retirement costs, workers' compensation insurance claims, and legal settlements.

⁽⁴⁾ Total passengers (fixed route and Paracruz) decreased by 7.0% due to a service reduction that was implemented on September 15, 2011, which resulted in 8.2% less service from September to late March.

⁽⁵⁾ Farebox Recovery Ratio is a standard transit performance indicator that is calculated by dividing passenger fares by total operating expenses and does not include depreciation.

- (6) Cost/Passenger is calculated by dividing total passengers by total (operating) expenses. Total expenses increased from prior year due to the GASB Statement No. 45 OPEB annual entry and increases in medical, retirement, workers' compensation, and legal settlement costs, while passenger count decreased as a result of the service reduction implemented in September 2011.
- (7) Cost/Hour is calculated by dividing total (operating) expenses by revenue hours. Total expenses increased over prior year due to the GASB Statement No. 45 OPEB annual entry and increases in medical, retirement, workers' compensation, and legal settlement costs, while revenue hours decreased as a result of the service reduction implemented in September 2011.
- (8) Cost/Mile is calculated by dividing total (operating) expenses by revenue miles. The increase from prior year is due to the GASB Statement No. 45 OPEB annual entry and increased medical, retirement, workers' compensation, and legal settlement costs, coupled with the drop in revenue miles resulting from service reductions implemented in September 2011.
- (9) The number of vehicles in the Active Fleet – Fixed-Route increased over prior year due to the purchase of eleven (11) 40-foot New Flyer compressed natural gas (CNG) fixed route buses that were purchased with capital grant funds from the award of an FTA State of Good Repair (SGR) grant.



BROWN ARMSTRONG
Certified Public Accountants

**INDEPENDENT AUDITOR’S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF BASIC FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

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We have audited the basic financial statements of the Santa Cruz Metropolitan Transit District as of and for the year ended June 30, 2012, and have issued our report thereon dated December 20, 2012. 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

Management of the Santa Cruz Metropolitan Transit District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Santa Cruz Metropolitan Transit District’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 Santa Cruz Metropolitan Transit District’s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Santa Cruz Metropolitan Transit District’s internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis.

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



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Compliance and Other Matters

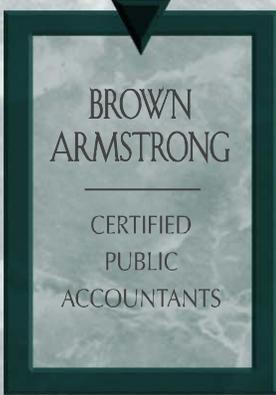
As part of obtaining reasonable assurance about whether the Santa Cruz Metropolitan Transit District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Directors, federal awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

*Brown Armstrong
Accountancy Corporation*

Bakersfield, California
December 20, 2012



BROWN ARMSTRONG

Certified Public Accountants

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

To the Board of Directors
Santa Cruz Metropolitan Transit District
Santa Cruz, California

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Compliance

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

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

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

Internal Control Over Compliance

Management of the Santa Cruz Metropolitan Transit District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Santa Cruz Metropolitan Transit District’s internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and



to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Santa Cruz Metropolitan Transit District's internal control over compliance.

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

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

Schedule of Expenditures of Federal Awards

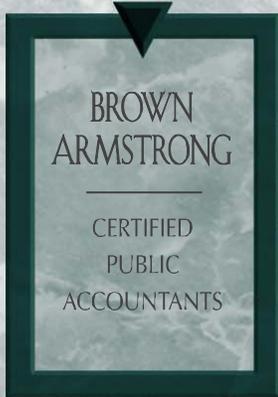
We have audited the financial statements of the Santa Cruz Metropolitan Transit District as of and for the year ended June 30, 2012, and have issued our report thereon dated December 20, 2012. Our audit was performed for the purpose of forming our opinion on the financial statements of the Santa Cruz Metropolitan Transit District. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information of management, the Board of Directors, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

Brown Armstrong
Accountancy Corporation

Bakersfield, California
December 20, 2012



BROWN ARMSTRONG
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH THE STATUTES, RULES, AND REGULATIONS OF THE CALIFORNIA TRANSPORTATION DEVELOPMENT ACT AND THE ALLOCATION INSTRUCTIONS AND RESOLUTIONS OF THE TRANSPORTATION COMMISSION

To the Board of Directors
Santa Cruz Metropolitan Transit District
Santa Cruz, California

We have audited the financial statements of the Santa Cruz Metropolitan Transit District as of and for the year ended June 30, 2012, and have issued our report thereon dated December 20, 2012. 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.

As part of obtaining reasonable assurance about whether the Santa Cruz Metropolitan Transit District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. Additionally, we performed tests to determine that allocations made and expenditures paid by the Santa Cruz Metropolitan Transit District were made in accordance with the allocation instructions and resolutions of the Santa Cruz Metropolitan Transit District and in conformance with the California Transportation Development Act. Specifically, we performed each of the specific tasks identified in the California Code of Regulations Sections 6666 and 6667 that are applicable to the Santa Cruz Metropolitan Transit District. In connection with our audit, nothing came to our attention that caused us to believe the Santa Cruz Metropolitan Transit District failed to comply with the Statutes, Rules, and Regulations of the California Transportation Development Act and the allocation instructions and resolutions of the Transportation Commission. 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.

Also as part of our audit, we performed tests of compliance to determine whether certain state funds were received and expended in accordance with the applicable bond act and state accounting requirements.

In November 2006, California Voters passed a bond measure enacting the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006. Of the \$19.925 billion of state general obligation bonds authorized, \$4 billion was set aside by the State as instructed by statute as the Public Transportation Modernization, Improvement, and Service Enhancement Account (PTMISEA). These funds are available to the California Department of Transportation for intercity rail projects and to transit operators in California for rehabilitation, safety or modernization improvements, capital service enhancements or expansions, new capital projects, bus rapid transit improvements, or for rolling stock procurement, rehabilitation, or replacement.

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During the fiscal year ended June 30, 2012, Santa Cruz METRO received \$13,501,970 from the State's PTMISEA funds for the purpose of construction of the Consolidated MetroBase Project. As of June 30, 2012, PTMISEA interest received and funds expended were verified in the course of our audit as follows:

Schedule of PTMISEA Bond 1B Funds For the Year Ended June 30, 2012	
Description	Amount
Balance – beginning of the year	\$ 430,416
Proceeds received:	
PTMISEA receipts	13,501,970
Interest earned	26,866
Expenses incurred:	
MetroBase Construction	(463,448)
Balance – end of year	<u>\$ 13,495,804</u>

This report is intended solely for the information and use of management, the California Department of Transportation, and the State Controller's Office and is not intended to be, and should not be, used by anyone other than these specified parties.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

*Brown Armstrong
Accountancy Corporation*

Bakersfield, California
December 20, 2012

FINDINGS AND QUESTIONED COSTS SECTION

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
JUNE 30, 2012**

I. Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness identified?	Yes	<input checked="" type="checkbox"/>	No
Significant deficiencies identified?	Yes	<input checked="" type="checkbox"/>	None reported
Noncompliance material to financial statements noted?	Yes	<input checked="" type="checkbox"/>	No

Federal Awards

Internal control over major federal programs:

Material weakness identified?	Yes	<input checked="" type="checkbox"/>	No
Reportable conditions identified that are not considered to be material weaknesses?	Yes	<input checked="" type="checkbox"/>	None reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133, Section .510(a)?	Yes	<input checked="" type="checkbox"/>	No
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Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Clusters</u>
20.500	Federal Transit Capital Investment Grants – Section 3
20.507	Federal Transit Formula Grants – Section 9

Dollar threshold used to distinguish type A and B programs: \$306,172

Auditee qualified as low risk auditee?	<input checked="" type="checkbox"/>	Yes	No
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II. Findings Relating to Financial Statements Required Under Generally Accepted Government Auditing Standards

None.

III. Federal Award Findings and Questioned Costs

None.

IV. State Award Findings and Questioned Costs

None.

V. A Summary of Prior Audit (all June 30, 2011) Findings and Current Year Status Follows

None.