

Klamath Falls
Urban Renewal Agency

*A component unit of the
City of Klamath Falls, Oregon*

Financial Statements

For the Fiscal Year Ended
June 30, 2011

KLAMATH FALLS URBAN RENEWAL AGENCY
 FINANCIAL STATEMENTS
 June 30, 2011

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INTRODUCTORY SECTION

KLAMATH FALLS URBAN RENEWAL AGENCY
 GENERAL INFORMATION
 LISTING OF PRINCIPAL DISTRICT OFFICIALS AND STAFF
 June 30, 2011

Elected Officials

		<u>Length of Service</u>
Mayor	Todd L. Kellstrom	8 yrs, 6 mos.
City Council Member	Irving "Bud" Hart	22 yrs, 6 mos.
City Council Member	William Adams	8 yrs, 6 mos.
City Council Member	Greg Taylor	6 mos.
City Council President	Dan Tofell	6 mos.
City Council Member	Trish Seiler	10 yrs, 6 mos.

Appointed Officials

		<u>Length of Time In This Position</u>	<u>Length of Employment with The City of Klamath Falls</u>
City Manager	Rick Whitlock	1 yr. 3 mos.	11 yrs, 1 mos.
City Attorney	Joanna Lyons-Antley	1 yr. 3 mos.	1 yr. 3 mos.

Appointed Directors

		<u>Length of Time In This Position</u>	<u>Length of Employment with The City of Klamath Falls</u>
Finance Director, Phyllis Shidler		8 yrs, 7 mos.	8 yrs, 7 mos.
Community Development Director, Sandra Fox		10 yrs, 9 mos.	12 yrs, 10 mos.

INDEPENDENT AUDITOR'S REPORT



824 Pine Street
Klamath Falls, OR 97601
(541) 884-4164
Fax: (541) 883-1232

A0611-51403-1

Certified Public Accountants

Independent Auditors' Report

Board of Directors
Klamath Falls Urban Renewal Agency
Klamath Falls, Oregon

We have audited the accompanying financial statements of the governmental activities, and each major fund of the Klamath Falls Urban Renewal Agency, as of and for the year ended June 30, 2011, which collectively comprise the Klamath Falls Urban Renewal Agency's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the entity's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, and each major fund of the Klamath Falls Urban Renewal Agency, as of June 30, 2011, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

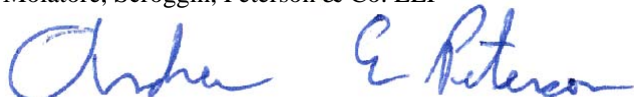
In accordance with *Government Auditing Standards*, we have issued our report dated January 3, 2012 on our consideration of the Klamath Falls Urban Renewal Agency's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant 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.

Management has not presented the management's discussion and analysis information required by accounting principles generally accepted in the United States of America to supplement, although not required to be a part of, the basic financial statements.

The budgetary comparison information on pages 19 through 21 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. The budgetary comparison 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Klamath Falls Urban Renewal Agency's basic financial statements. The other supplementary schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The other supplementary schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Molatore, Scroggin, Peterson & Co. LLP



Andrew E. Peterson, Partner

Klamath Falls, Oregon
January 3, 2012

BASIC FINANCIAL STATEMENTS

KLAMATH FALLS URBAN RENEWAL AGENCY
STATEMENT OF NET ASSETS
June 30, 2011

ASSETS	<u>Governmental Activities</u>
Current Assets:	
Accounts receivable	\$ 1,685
Taxes receivable	149,943
Interest receivable	1,765
Inventories	26,444
Temporarily restricted assets	
Cash and cash equivalents	<u>86,183</u>
Total Current Assets	<u>266,020</u>
Noncurrent Assets:	
Capital assets (net of accumulated depreciation)	
Land	245,030
Construction in progress	367,849
Buildings and system	1,820,777
Infrastructure	<u>298,056</u>
Total Noncurrent Assets	<u>2,731,712</u>
Total Assets	<u>2,997,732</u>
LIABILITIES	
Current Liabilities:	
Accounts payable	1,820
Leases / loans payable	<u>1,776,279</u>
Total Current Liabilities	<u>1,778,099</u>
Noncurrent Liabilities:	
Leases / Loans payable	<u>148,721</u>
Total Noncurrent Liabilities	<u>148,721</u>
Total Liabilities	<u>1,926,820</u>
NET ASSETS	
Invested in capital assets, net of related debt	2,331,712
Restricted for capital	164,045
Unrestricted	<u>(1,424,845)</u>
Total Net Assets	<u><u>\$ 1,070,912</u></u>

The notes to the financial statements are an integral part of this statement.

KLAMATH FALLS URBAN RENEWAL AGENCY
STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2011

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	
Governmental Activities:				
General government	\$ 208,009	\$ 52,738	\$	\$ (155,271)
Interest on long-term debt	<u>111,143</u>			<u>(111,143)</u>
Total Government Activities	<u>\$ 319,152</u>	<u>\$ 52,738</u>	<u>\$ -</u>	<u>\$ (266,414)</u>

General Revenues:

Property taxes	1,046,715
Unrestricted investment earnings	6,989
Loss on donation of capital assets	<u>(14,750)</u>
Total General Revenues	<u>1,038,954</u>
Change in Net Assets	<u>772,540</u>
Net Assets - Beginning	341,360
Restatement and prior period adjustments	<u>(42,988)</u>
Net Assets - Beginning as restated	298,372
Net Assets - Ending	<u>\$ 1,070,912</u>

The notes to the financial statements are an integral part of this statement.

KLAMATH FALLS URBAN RENEWAL AGENCY
BALANCE SHEET
GOVERNMENT FUNDS
June 30, 2011

	Downtown Urban Renewal Fund	Lakefront Urban Renewal Fund	Town Center Urban Renewal Fund	Total Governmental Funds
ASSETS				
Receivables				
Accounts	\$ 1,685	\$	\$	\$ 1,685
Taxes	107,248	15,685	27,010	149,943
Interest	1,258	185	322	1,765
Inventories	26,444			26,444
Temporarily restricted assets				
Cash and cash equivalents	55,674	10,927	19,582	86,183
Total Assets	\$ 192,309	\$ 26,797	\$ 46,914	\$ 266,020
LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable	\$ 1,820	\$	\$	\$ 1,820
Unearned revenue	90,555	13,172	22,842	126,569
Total Liabilities	92,375	13,172	22,842	128,389
Fund balances:				
Nonspendable	26,444			26,444
Restricted	73,490	13,625	24,072	111,187
Total Fund Balances	99,934	13,625	24,072	137,631
Total Liabilities and Fund Balances	\$ 192,309	\$ 26,797	\$ 46,914	
Amounts reported for governmental activities in the statement of net assets are different because:				
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.				2,731,712
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.				126,569
Long-term liabilities, including notes payable, are not due and payable in the current period and therefore not reported in the funds.				(1,925,000)
Net assets of governmental activities				\$ 1,070,912

The notes to the financial statements are an integral part of this statement.

KLAMATH FALLS URBAN RENEWAL AGENCY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the Year Ended June 30, 2011

	Downtown Urban Renewal Fund	Lakefront Urban Renewal Fund	Town Center Urban Renewal Fund	Total Governmental Funds
Revenues				
Taxes	\$ 739,937	\$ 111,690	\$ 178,161	\$ 1,029,788
Charges for services	52,677			52,677
Investment income	5,093	728	1,168	6,989
Miscellaneous revenues	61			61
Total Revenues	<u>797,768</u>	<u>112,418</u>	<u>179,329</u>	<u>1,089,515</u>
Expenditures				
Current:				
General government	134,633			134,633
Capital outlay:				
General government	16,741	14,750		31,491
Highways and streets	37,511			37,511
Debt service:				
Principal	705,500	120,000	150,000	975,500
Interest	33,246	10,713	67,184	111,143
Total Expenditures	<u>927,631</u>	<u>145,463</u>	<u>217,184</u>	<u>1,290,278</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(129,863)</u>	<u>(33,045)</u>	<u>(37,855)</u>	<u>(200,763)</u>
Other Financing Sources (Uses)				
Issuance of debt	105,500			105,500
Total Other Financing Sources and Uses	<u>105,500</u>			<u>105,500</u>
Net Change in Fund Balances	<u>(24,363)</u>	<u>(33,045)</u>	<u>(37,855)</u>	<u>(95,263)</u>
Fund Balances - Beginning	167,285	46,670	61,927	275,882
Prior period adjustment	(42,988)			(42,988)
Fund Balances - Beginning, as restated	<u>124,297</u>	<u>46,670</u>	<u>61,927</u>	<u>232,894</u>
Fund Balances - Ending	<u>\$ 99,934</u>	<u>\$ 13,625</u>	<u>\$ 24,072</u>	<u>\$ 137,631</u>

The notes to the financial statements are an integral part of this statement.

KLAMATH FALLS URBAN RENEWAL AGENCY
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2011

Amounts reported for governmental activities in the statement of activities (page 4) are different because:

Net change in fund balances - total governmental funds (page 6)	\$	(95,263)
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlay in the current period.		(4,374)
The net effect of various miscellaneous transactions involving capital assets (i.e. sales, trade-ins, and donations) is to decrease net assets.		(14,750)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.		16,927
The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.		870,000
		870,000
Change in net assets of governmental activities (page 4)	\$	772,540

The notes to the financial statements are an integral part of this statement.

NOTES TO THE FINANCIAL STATEMENTS

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The Klamath Falls Urban Renewal Agency (Agency), was organized in 1989 under the provisions of ORS Chapter 457 as the urban renewal agency in the City of Klamath Falls, Oregon (City), responsible for implementing various public improvement projects as identified in the revitalization plan of the City.

The “tax increment financing” method is being used to provide funds for the agency. Under this method, a base year value within the urban renewal area is established for the duration of the urban renewal program. Any increase in the assessed value over the base year cannot be used by the assessor to compute tax rates for the local taxing bodies. The assessor computes the tax rate on the base year value of the area then applies that rate to the increase in assessed value. The tax on the increased value can be used by the agency only to pay indebtedness incurred to finance the urban renewal projects.

The following is a summary of significant accounting policies utilized by the agency in the preparation of the accompanying financial statements.

Reporting entity

The agency’s governing body is identical to that of the City, and because the services of the agency are for the benefit of the City, the agency has been determined under accounting standards generally accepted in the United States of America to be a blended component unit of the City. As a result, the agency’s financial statements are blended with those of the City by including them in the appropriate statements and schedules of the City’s Comprehensive Annual Financial Report. Copies of which may be obtained from the City’s Finance Director, City of Klamath Falls, 500 Klamath Avenue, Klamath Falls, OR 97601.

Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the activities of the primary agency and its component units. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Major individual governmental funds are reported as separate columns in the fund financial statements.

Measurement focus, basis of accounting, and financial statement presentation

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the agency considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, are recorded only when payment is due.

Property taxes, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the agency.

The agency reports the following major governmental funds:

The *downtown urban renewal fund* accounts for public improvement projects in a district encompassing downtown Klamath Falls.

The *lakefront urban renewal fund* accounts for public improvement projects in a district encompassing the old Modoc Mill site and future Timber Mill Shores development.

The *town center urban renewal fund* accounts for public improvement projects in a district encompassing the old Klamath Mall site and future Town Center development.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The agency has elected not to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes where the amounts are reasonably equivalent in value to the interfund services provided. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

When both restricted and unrestricted resources are available for use, it is the agency's policy to use restricted resources first, then unrestricted resources as they are needed.

Deposits and investments

The agency participates in the City's cash and investment pool.

The agency's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. The Agency participates in the Oregon State Treasurer's Local Government Investment Pool (LGIP), an open-ended, no-load diversified portfolio created under ORS 294.805 to 294.895.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The LGIP is administered by the State Treasurer and the Oregon Investment Council with the advice of the Oregon Short-Term Bond Fund Board. The Oregon State Treasurer's Office has calculated the fair value of the underlying investments of the LGIP and the Government's share of fair value is the same as the reported value.

Investments for the agency are reported at fair value.

Receivables and payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and not expendable available financial resources.

All trade and property tax receivables are shown net of an allowance for uncollectibles. Allowance for uncollectibles on trade accounts receivables is based on the agency's expected net write-offs for the next year based upon past history. No allowance for uncollectibles has been provided for property taxes as the agency considers all taxes fully collectible.

Property taxes become a lien against the property, as of July 1, in the year in which due and are assessed in October through billing by the county to the property owner. Payments are due in three equal installments on November 15, February 15 and May 15 with a 3% discount available for payment in full on November 15. Taxes unpaid and outstanding on May 16 are considered delinquent and are subject to lien, and penalties and interest are assessed.

Inventories and prepaid items

All inventories are valued at cost using the first-in/first-out (FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Capital assets

Capital assets, which include property, buildings, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the governmental activities column in the government-wide financial statements. Capital assets are defined by the agency as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year. The agency reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets, (i.e., those reported by the governmental activities) the agency chose to include all such items regardless of their acquisition date or amount. The agency was able to estimate historical cost for the initial reporting of these assets through backtrending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using an appropriate price-level index to deflate the cost to acquisition year or estimated acquisition year).

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

As the agency constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. In the case of donations the agency values these capital assets at the estimated fair value of the item at the date of its donation.

The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate.

Property, buildings, and equipment of the agency are depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	40
Building improvements	25
Public domain infrastructure	25-50

Long-term obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the governmental activities statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method, which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Fund balance

In accordance with Government Accounting Standards Board 54, Fund Balance Reporting and Governmental Fund Type Definitions, the City classifies governmental fund balances as follows:

- Non-spendable – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.
- Restricted – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.
- Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end.
- Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund Balance may be assigned by the Finance Director.
- Unassigned includes positive fund balance within the General Fund which has not been classified within the above mentioned categories and negative fund balances in other governmental funds.

KLAMATH FALLS URBAN RENEWAL AGENCY
 NOTES TO THE FINANCIAL STATEMENTS
 June 30, 2011

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of Estimates

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

NOTE 2 – RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets

The governmental fund balance sheet includes a reconciliation between *fund balance – total governmental funds* and *net assets – governmental-activities* as reported in the government-wide statement of net assets. The difference results primarily from the long-term economic focus of the statement of net assets versus the current financial resources focus of the governmental fund balance sheet. Some of the elements of the reconciliation are as follows:

The first element of the reconciliation are capital related items. When capital assets (property, plant, equipment) that are to be used in governmental activities are purchased or constructed, the cost of those assets are reported as expenditures in governmental funds. However the statement of net assets includes those capital assets among the assets of the agency as a whole. The details of this \$2,731,712 difference are as follows:

Cost of capital assets	\$2,881,828
Accumulated depreciation	<u>(150,116)</u>
Net adjustment to increase <i>fund balance – total governmental funds</i> to arrive at <i>net assets – governmental activities</i>	<u>\$2,731,712</u>

The second element of that reconciliation explains that “other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.” The detail of this \$126,569 difference is as follows:

Property taxes	<u>\$ 126,569</u>
Net adjustment to increase <i>fund balance – total governmental funds</i> to arrive at <i>net assets – governmental activities</i>	<u>\$ 126,569</u>

The third element of that reconciliation explains that “long-term liabilities, including bonds, are not due and payable in the current period and therefore are not reported in the funds.” The details of this \$(1,925,000) difference are as follows:

Notes payable	<u>\$(1,925,000)</u>
Net adjustment to reduce <i>fund balance – total governmental funds</i> to arrive at <i>net assets – governmental activities</i>	<u>\$(1,925,000)</u>

Explanation of certain differences between the governmental fund statement of revenues, expenditures, and changes in fund balances and the government-wide statement of activities

The governmental fund statement of revenues, expenditures, and changes in fund balances includes a reconciliation between *net changes in fund balance – total governmental funds* and *changes in net assets of governmental activities* as reported in the government-wide statement of activities.

KLAMATH FALLS URBAN RENEWAL AGENCY
 NOTES TO THE FINANCIAL STATEMENTS
 June 30, 2011

NOTE 2 – RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

(continued)

The first element of that reconciliation explains that “Governmental funds report capital outlays as expenditures. However, in the statement of activities the costs of those assets is allocated over their estimated useful lives and reported as depreciation expense.” The details of this \$(4,374) difference are as follows:

Capital outlay	\$ 69,002
Depreciation expense	<u>(73,376)</u>
Net adjustment to decrease <i>net changes in fund balances – total governmental funds</i> to arrive at <i>changes in net assets of governmental activities</i>	<u>\$ (4,374)</u>

The second element of that reconciliation states that “The net effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) is to decrease net assets.” The details of this \$(14,750) difference are as follows:

Donation of capital asset	<u>\$ (14,750)</u>
---------------------------	--------------------

The third element of that reconciliation states that “revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds”. The detail of this \$16,927 difference is as follows:

Property taxes	<u>\$ 16,927</u>
Net adjustment to increase <i>net changes in fund balances – total governmental funds</i> to arrive at <i>changes in net assets of governmental activities</i>	<u>\$ 16,927</u>

The fourth and final element of that reconciliation states that “the issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effects of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.”

The details of this \$870,000 difference are as follows:

Debt issued or incurred:	
Issuance of notes payable	\$ (105,500)
Principal repayments:	
Notes payable repayments	<u>975,500</u>
Net adjustment to decrease <i>net changes in fund balances – total governmental funds</i> to arrive at <i>changes in net assets of governmental activities</i>	<u>\$ 870,000</u>

NOTE 3 – STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgetary information

The agency budgets all funds. A City Council order authorizing appropriations for each fund sets the level by which expenditures cannot legally exceed appropriations. Either expenditures by department within funds or total personal services, materials and services, capital outlay and other expenditures by fund are the levels of control established by the City Council order. The detail budget document, however, is required to contain more specific, detailed information for the above mentioned expenditure categories.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 3 – STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY (continued)

Unexpected additional resources or appropriations may be added to the budget through the use of a supplemental budget. A supplemental budget requires hearings before the public, publications in newspapers, and approval by the City Council. Original and supplemental budgets may be modified by the use of appropriation transfers between the levels of control. Such transfers require approval by passing a Council resolution authorizing the transfer. All budget amendments are subject to the limitations put forth in the Oregon Revised Statutes Chapters 294.305 through 294.565 (Oregon Budget Law). Supplemental appropriations, permitted by Oregon Budget Law, were authorized by the City Council during the fiscal year. The agency does not use encumbrances.

Annual budgets are adopted generally following the modified accrual basis of accounting with the exception that interfund loans and repayments are budgeted similar to other debt transactions. The nature and amount of all significant adjustments necessary to convert data prepared on a basis consistent with generally accepted accounting principles to a budgetary basis are noted on the budget to actual statements included in the financial statements. All annual appropriations lapse at fiscal year end.

NOTE 4 –DEPOSITS AND INVESTMENTS

Cash and cash equivalents are reflected on the Statement of Net Assets as follows:

Cash and cash equivalents	<u>\$ 86,183</u>
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Cash and cash equivalents are comprised of the following at June 30, 2011:

Deposits with financial institutions	<u>\$ 658</u>
--------------------------------------	---------------

As of June 30, 2011, the agency had the following investments:

State Treasurer’s Investment Pool	<u>\$ 85,525</u>
-----------------------------------	------------------

CUSTODIAL CREDIT RISK – In the case of deposits, this is the risk, that in the event of a bank failure, the agency’s deposits may not be returned to it. The agency’s deposit policy is in accordance with ORS.295. All deposits are collateralized with eligible securities in amounts determined by the Office of the State Treasurer (OST). The agency’s deposit policy requires that all deposits are covered by the Federal Deposit Insurance Corporation (FDIC) and/or are collateralized as required by compliance with ORS 295. At June 30, 2011 the agency’s deposits were fully insured.

INTEREST RATE RISK – In accordance with its investment policy, the agency manages its exposure to declines in fair values by limiting the duration of its investments for operating purposes to eighteen months and nonoperating investments may be invested for up to ten years. Management has elected to maintain shorter durations except where directed to longer term investments by bond indentures.

CREDIT RISK – Oregon Revised Statutes, Chapter 294, authorize the agency to invest in obligations of the U.S. Treasury, U.S. Government agencies and instrumentalities, bankers’ acceptances guaranteed by an Oregon financial institution, repurchase agreements, State of Oregon Local Government Investment Pool, certain high grade commercial paper, and various interest bearing bonds of Oregon municipalities, among others. The agency’s investment portfolio as of June 30, 2011 is representative of the types of investments made throughout the year. The agency’s investments in the state treasurer’s investment pool are unrated. Investments in the LGIP are included in the Oregon Short-Term Fund, which is not registered with the U.S. Securities and Exchange Commission as an investment company. The fair value of the LGIP is the same amount as the value of the pool shares. Investments in the Short-Term Fund are governed by ORS 294.135, Oregon Investment Council, and portfolio guidelines issued by the Oregon Short-Term Fund Board.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 4 – DEPOSITS AND INVESTMENTS (continued)

CONCENTRATION OF CREDIT RISK – The agency has adopted the policies as described in the Oregon Revised Statutes, Chapter 294, as it pertains to investments. The policy does not allow for an investment in any one issuer that is in excess of five percent of the agency’s total investments.

CUSTODIAL CREDIT RISK – For an investment, this is the risk that, in the event of the failure of the counterparty, the agency will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. None of the agency’s investments are subject to custodial credit risk.

NOTE 5 – CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2011 was as follows:

	Beginning Balance	Increases	Decreases	Donation	Ending Balance
Governmental activities:					
Capital assets, not being depreciated:					
Land	\$ 245,030	\$	\$	\$	\$ 245,030
Construction in progress	<u>347,385</u>	<u>52,262</u>	<u>(17,048)</u>	<u>(14,750)</u>	<u>367,849</u>
Total capital assets, not being depreciated	<u>592,415</u>	<u>52,262</u>	<u>(17,048)</u>	<u>(14,750)</u>	<u>612,879</u>
Capital assets, being depreciated:					
Buildings	1,921,225	16,740			1,937,965
Infrastructure	<u>313,937</u>	<u>17,048</u>			<u>330,985</u>
Total capital assets being depreciated	<u>2,235,162</u>	<u>33,788</u>	<u>-</u>		<u>2,268,950</u>
Less accumulated depreciation for:					
Buildings	(52,133)	(65,055)			(117,188)
Infrastructure	<u>(24,608)</u>	<u>(8,321)</u>			<u>(32,929)</u>
Total accumulated depreciation	<u>(76,741)</u>	<u>(73,376)</u>	<u>-</u>		<u>(150,117)</u>
Total capital assets being depreciated,	<u>2,158,421</u>	<u>(39,588)</u>	<u>-</u>		<u>2,118,833</u>
Governmental activities capital assets, net	<u>\$ 2,750,836</u>	<u>\$ 12,674</u>	<u>\$ (17,048)</u>	<u>\$ (14,750)</u>	<u>\$ 2,731,712</u>

Depreciation expense was charged to functions/programs of the government as follows:

Governmental activities:

General Government \$ 73,376

NOTE 6 – OPERATING LEASES

The government leases land and buildings under non-cancelable operating leases to other parties. The cost of the leased asset was \$1,007,741 and the carrying value was \$946,803. Future minimum rental payments to be received on leases are as follows for the years ended June 30:

2012	\$ 63,330
2013	33,942
2014	<u>7,377</u>
Total	<u>\$ 104,649</u>

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 6 – OPERATING LEASES (continued)

Minimum future rentals do not include contingent rentals that may be received under certain leases of land and buildings, because payments are based upon usage, or increases based upon changes in the consumer price index.

NOTE 7 – LONG-TERM LIABILITIES

Interest expense recorded in the statement of activities for governmental activities was \$111,143.

The government does not sell receivables or future revenues. The government does however pledge revenues to collateralize debt until the debt is fully repaid. The following information discloses the government's pledged revenues:

Downtown Urban Renewal

The government has pledged future tax increment revenues to repay a renewable loan of \$1.45 million from South Valley Bank and Trust received in April 2009. From April 2009 to June 2011 the City has borrowed \$1,893,500 and paid back \$1,493,500 in principal. The loan was used to remodel 205 Riverside in the Downtown Urban Renewal District as a visitor information center. Monthly payments of interest are required to be paid at a variable interest of prime plus 1.375% (currently 4.625%) until maturity on July 1, 2011, at which time the principal will be due in full. The interest rate is based on the Lender's Prime Rate (the "Index") and will not change more often than daily. The government will pay down the loan by 100% of the increment property taxes received. The loan will be renewed on July 1, 2011. The loan is payable solely from the property tax increment revenues of properties within the district boundaries. \$739,937 in property taxes were available to pay \$705,500 of principal and \$33,246 of interest on the loan in the current year. Total principal and interest remaining on the loan at June 30, 2011 is \$400,051.

Lakefront Urban Renewal

The government has pledged future tax increment revenues to repay \$582,500 for a loan from South Valley Bank and Trust received in February 2007, due and payable in January of 2011. In February of 2011 the government renewed the loan for \$225,000 with payments due in two annual installments of \$82,105 and one irregular payment of \$77,181. The funds from the loan were used to finance storm drains, water system, sanitary sewer and geothermal heat for the Lakefront Urban Renewal District. The interest rate is subject to change annually based on prime plus 1.50% (currently 4.750%) in accordance with the highest prime rate as published in the West Coast Edition of the Wall Street Journal (the "Index"). The loan is payable solely from the property tax increment revenues of properties within the district boundaries. For the current year, principal and interest paid and total incremental property tax revenues were \$130,713 and \$111,690 respectively. Total principal and interest remaining on the loan at June 30, 2011 is \$241,391.

Town Center Urban Renewal

The government has pledged future tax increment revenues to repay \$2.5 million for an annual renewable loan from South Valley Bank and Trust. The funds from the loan were used to finance improvements to the Town Center Urban Renewal District. From March 2006 to June 2011 the government has borrowed \$1.825 million and paid back \$525 thousand in principal. Monthly payments of interest only will be due with a variable interest of prime plus 1.375% (currently 4.625%). The interest rate is based on the lender's Prime Rate (the "Index") and will not change more often than daily. The government uses 100% of the increment property taxes to pay the loan. If the district continues to build out and assessed increment taxes increase, the loan will be renewed annually until the full \$2.5 million is borrowed. At that time the loan will be renewed and will be payable solely from the property tax increment revenues of properties within the district boundaries. With no additional borrowing, current incremental property taxes will sustain a nine year loan even if the district has no further improvements. For the current year, principal and interest paid and total incremental property tax revenues were \$217,184 and \$178,161 respectively. Total principal and interest remaining on the loan at June 30, 2011 is \$1,302,505.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 7 – LONG-TERM LIABILITIES (continued)

Long-term liability activity for the year ended June 30, 2011:

Governmental Activities Bonds and Notes Payable

	Balance June 30, 2010	Additions	Reductions	Balance June 30, 2011	Due Within One Year
SVBT - Downtown Urban Renewal	\$ 1,000,000	\$ 105,500	\$ 705,500	\$ 400,000	\$ 400,000
SVBT - Lakefront Urban Renewal	345,000	-	120,000	225,000	76,279
SVBT - Town Center Urban Renewal	1,450,000		150,000	1,300,000	1,300,000
Total bonds and notes payable	<u>2,795,000</u>	<u>105,500</u>	<u>975,500</u>	<u>1,925,000</u>	<u>1,776,279</u>
Governmental activities long-term liabilities	<u>\$ 2,795,000</u>	<u>\$ 105,500</u>	<u>\$ 975,500</u>	<u>\$ 1,925,000</u>	<u>\$ 1,776,279</u>

Long-term Liabilities

Other long-term liabilities debt service requirements to maturity are as follows:

	2012	2013	2014	Total
SVBT - Downtown Urban Renewal				
Principal	\$ 400,000	\$	\$	\$ 400,000
Interest	51			51
SVBT - Lakefront Urban Renewal				
Principal	76,279	75,041	73,680	225,000
Interest	5,826	7,064	3,501	16,391
SVBT - Town Center Urban Renewal				
Principal	1,300,000			1,300,000
Interest	2,505			2,505
Total long-term liabilities	<u>\$ 1,784,661</u>	<u>\$ 82,105</u>	<u>\$ 77,181</u>	<u>\$ 1,943,947</u>

NOTE 8 – CONTINGENT LIABILITIES

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the agency expects such amounts, if any, to be immaterial.

NOTE 9 – RISK MANAGEMENT

The agency is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters. The agency is covered under the City's insurance policies. The City carries commercial insurance for all risks of loss described. Settlements have not exceeded coverages for each of the past three fiscal years.

KLAMATH FALLS URBAN RENEWAL AGENCY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2011

NOTE 10 – RELATED PARTY TRANSACTIONS

Transactions with the Agency for the year ended June 30, 2011 are as follows:

Expenses:	
Wastewater charges	\$ 362
Water charges	1,023
Street lighting charges	48
Administrative service charge	69,750
Maintenance service charge	<u>1,321</u>
 Total Expenses	 <u>\$ 72,504</u>

NOTE 11 – PRIOR PERIOD ADJUSTMENT

The government entered into an agreement with the State of Oregon Department of Transportation to receive Federal Highway Administration funds under the Transportation Enhancement Program, Title 23, United States Code, which incorporated SAFETEA-LU. This agreement was entered into in December of 2005 and was administered by the Oregon Department of Transportation until completion in February of 2011.

In February 2011 the government was notified that the Oregon Department of Transportation had erroneously over reported the amount of participation from the Federal Highway Administration in the fiscal year ended June 30, 2010. The prior period adjustment in the amount of \$42,988 reflects a decrease of intergovernmental revenues in the Downtown Urban Renewal Fund for the prior fiscal year and decreases the beginning fund balance for the current fiscal year ended June 30, 2011.

NOTE 12 – NEW PRONOUNCEMENTS

The Governmental Accounting Standards Board issued statement No. 62, *Codification of Accounting and Financial Reporting Guidance in Pre-November 30 1989 FASB and AICPA*, which incorporates certain pre-November 30, 1989 FASB and AICPA Pronouncements into the GASB literature. The benefits are that the applicable literature is easier to locate and contradictory literature should be eliminated. Accounting changes adopted to conform to the provisions of the Statement should be applied retroactively by restating financial statements, if practical, for all prior periods presented. The requirements of this standard will be implemented by the government in the fiscal year ending June 30, 2012. The government has not yet determined the impact of the implementation of this statement on its financial statements.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF KLAMATH FALLS, OREGON
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
DOWNTOWN URBAN RENEWAL FUND
For the Year Ended June 30, 2011

Schedule A-1

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues				
Taxes	\$ 732,900	\$ 732,900	\$ 739,937	\$ 7,037
Charges for services	35,375	35,375	52,677	17,302
Investment income	2,900	2,900	5,093	2,193
Miscellaneous revenues			61	61
Total Revenues	771,175	771,175	797,768	26,593
Expenditures				
Downtown urban renewal agency				
Materials and services	129,075	135,075	134,633	442
Capital outlay	225,000	219,000	54,252	164,748
Debt service	739,175	739,175	738,746	429
Contingency	33,525	33,525		33,525
Total Expenditures	1,126,775	1,126,775	927,631	199,144
Excess (Deficiency) of Revenues Over (Under) Expenditures	(355,600)	(355,600)	(129,863)	225,737
Other Financing Sources (Uses)				
Issuance of debt	325,600	325,600	105,500	(220,100)
Excess (Deficiency) of Revenues and Other Sources Over (Under) Expenditures and Other (Uses)	(30,000)	(30,000)	- (24,363)	5,637
Fund Balance - Beginning	30,000	30,000	167,285	137,285
Prior period adjustment			(42,988)	(42,988)
Fund Balance - Beginning as restated	30,000	30,000	124,297	94,297
Fund Balance - Ending	\$ -	\$ -	\$ 99,934	\$ 99,934

The notes to the financial statements are an integral part of this statement

CITY OF KLAMATH FALLS, OREGON
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
LAKEFRONT URBAN RENEWAL FUND
For the Year Ended June 30, 2011

Schedule A-2

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues				
Taxes	\$ 121,175	\$ 121,175	\$ 111,690	\$ (9,485)
Investment income			728	728
Total Revenues	121,175	121,175	112,418	(8,757)
Expenditures				
Lakefront urban renewal agency				
Materials& Services	15,000	-		-
Capital Outlay		15,000	14,750	250
Debt service	132,175	132,175	130,713	1,462
Contingency	3,800	3,800		3,800
Total Expenditures	150,975	150,975	145,463	5,512
Excess (Deficiency) of Revenues Over (Under) Expenditures	(29,800)	(29,800)	(33,045)	(3,245)
Fund Balance - Beginning	29,800	29,800	46,670	16,870
Fund Balance - Ending	\$ -	\$ -	\$ 13,625	\$ 13,625

The notes to the financial statements are an integral part of this statement.

CITY OF KLAMATH FALLS, OREGON
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
TOWN CENTER URBAN RENEWAL FUND
For the Year Ended June 30, 2011

Schedule A-3

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues				
Taxes	\$ 245,975	\$ 245,975	\$ 178,161	\$ (67,814)
Investment income	300	300	1,168	868
Total Revenues	<u>246,275</u>	<u>246,275</u>	<u>179,329</u>	<u>(66,946)</u>
Expenditures				
Town Center urban renewal agency				
Materials and services	725,000	725,000		725,000
Debt service	246,050	246,050	217,184	28,866
Contingency	<u>51,575</u>	<u>51,575</u>		<u>51,575</u>
Total Expenditures	<u>1,022,625</u>	<u>1,022,625</u>	<u>217,184</u>	<u>805,441</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	(776,350)	(776,350)	(37,855)	738,495
Other Financing Sources (Uses)				
Issuance of debt	<u>725,000</u>	<u>725,000</u>	-	<u>725,000</u>
Excess (Deficiency) of Revenues and Other Sources Over (Under) Expenditures and Other (Uses)	(51,350)	(51,350)	(37,855)	13,495
Fund Balance - Beginning	<u>51,350</u>	<u>51,350</u>	<u>61,927</u>	<u>10,577</u>
Fund Balance - Ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 24,072</u>	<u>\$ 24,072</u>

The notes to the financial statements are an integral part of this statement.

OTHER SUPPLEMENTARY SCHEDULE

KLAMATH FALLS URBAN RENEWAL AGENCY
SCHEDULE OF PROPERTY TAX TRANSACTIONS
For the Year Ended June 30, 2011

Schedule B-1

Fiscal Year	Assessor's Current Levy and Balances July 1, 2010	Discounts/ Adjustments	Taxes Collected	Balance Uncollected June 30, 2011	Interest Collected (Memo Only)
2010-2011	\$ 1,076,682	\$ (27,705)	\$ 972,712	\$ 76,265	\$ 383
Prior years					
2009-10	76,093	42	39,438	36,697	1,341
2008-09	29,647	(1,093)	8,524	20,030	991
2007-08	16,881	(264)	6,784	9,833	879
2006-07	7,081	(251)	4,269	2,561	659
2005-06	1,199	(166)	291	742	121
2004-05	910	(195)	152	563	91
2003-04 and Prior	3,616	(334)	30	3,252	88
 Total - Prior Years	 135,427	 (2,261)	 59,488	 73,678	 4,170
 Total	 <u>\$ 1,212,109</u>	 <u>\$ (29,966)</u>	 <u>\$ 1,032,200</u>	 <u>\$ 149,943</u>	 <u>\$ 4,553</u>

Summary by Fund

Downtown Urban Renewal Fund	107,248
Lakefront Urban Renewal Fund	15,685
Town Center Urban Renewal Fund	27,010
 Total	 <u>\$ 149,943</u>

GOVERNMENT AUDITING STANDARDS SECTION



824 Pine Street
Klamath Falls, OR 97601
(541) 884-4164
Fax: (541) 883-1232

Certified Public Accountants

**Report on Compliance and on Internal Control over Financial Reporting
Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards***

Board of Directors
Klamath Falls Urban Renewal Agency
Klamath Falls, Oregon

We have audited the basic financial statements of Klamath Falls Urban Renewal Agency as of and for the year ended June 30, 2011 and have issued our report thereon dated January 3, 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.

Compliance

As part of obtaining reasonable assurance about whether Klamath Falls Urban Renewal Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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 *Governmental Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Klamath Falls Urban Renewal Agency's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Klamath Falls Urban Renewal Agency's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Klamath Falls Urban Renewal Agency's internal control over financial reporting.

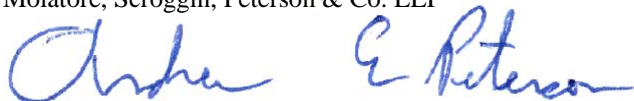
A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination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

Our consideration of the 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 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.

We noted certain other matters that we reported to management of the Klamath Falls Urban Renewal Agency, in a separate letter dated January 3, 2012.

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

Molatore, Scroggin, Peterson & Co. LLP

A handwritten signature in blue ink, appearing to read "Andrew E. Peterson", is written over a horizontal line.

Andrew E. Peterson
Klamath Falls, Oregon
January 3, 2012

**AUDIT COMMENTS AND DISCLOSURES
REQUIRED BY STATE REGULATIONS SECTION**



824 Pine Street
Klamath Falls, OR 97601
(541) 884-4164
Fax: (541) 883-1232

Certified Public Accountants

Report on Compliance and Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Oregon Minimum Standards*

Board of Directors
Klamath Falls Urban Renewal Agency
Klamath Falls, Oregon

We have audited the basic financial statements of Klamath Falls Urban Renewal Agency as of and for the year ended June 30, 2011, and have issued our report thereon dated January 3, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of Minimum Standards for Audits of Oregon Municipal Corporations, prescribed by the Secretary of State.

Compliance

As part of obtaining reasonable assurance about whether Klamath Falls Urban Renewal Agency's basic financial statements are free of material misstatements, we performed tests of its compliance with certain provisions of laws, regulations, contracts, grants including provisions of Oregon Revised Statutes as specified in Oregon Administrative Rules OAR 162-10-0000 to 162-10-0330, as set forth below, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

- The accounting records and related internal control structure.
- The use of various depositories to secure the deposit of public funds.
- The requirements relating to debt.
- The requirements relating to the preparation, adoption and execution of the annual budgets for fiscal years 2011 and 2012.
- The requirements relating to insurance and fidelity bond coverage.
- The appropriate laws, rules and regulations pertaining to programs funded wholly or partially by other government agencies.
- The requirements pertaining to the investment of public funds.
- The requirements pertaining to the awarding of public contracts and the construction of public improvements.

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 that are required to be reported under Minimum Standards for Audits of Oregon Municipal Corporations, prescribed by the Secretary of State.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Klamath Falls Urban Renewal Agency's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of Klamath Falls Urban Renewal Agency's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Klamath Falls Urban Renewal Agency's internal control over financial reporting.

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

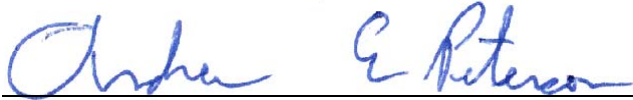
Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this

section and was not designed to identify all deficiencies in internal control 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.

We noted certain other matters that we reported to management of the Klamath Falls Urban Renewal Agency, in a separate letter dated January 3, 2012.

This report is intended solely for the information of management, City Council, and the Secretary of State, Audits Division and is not intended to be and should not be used by anyone other than those specified parties.

Molatore, Scroggin, Peterson & Co. LLP



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Klamath Falls, Oregon
January 3, 2012