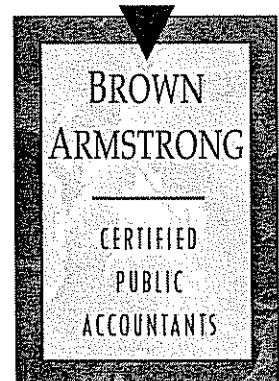


SANTA CRUZ METROPOLITAN TRANSIT DISTRICT

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

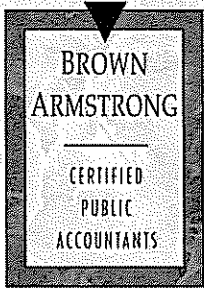
JUNE 30, 2001 AND 2000



**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
JUNE 30, 2001 AND 2000**

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INDEPENDENT AUDITOR'S REPORT

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 (the District), as of June 30, 2001, as listed in the table of contents. These financial statements are the responsibility of the Santa Cruz Metropolitan Transit District's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit. The financial statements for the year ended June 30, 2000 were audited by other auditor's whose report dated September 8, 2000 was unqualified.

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 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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Santa Cruz Metropolitan Transit District, as of June 30, 2001, and the results of its operations and the cash flows 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 also issued our report dated September 20, 2001 on our consideration of the Santa Cruz Metropolitan Transit District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Our audit was performed for the purpose of forming an opinion on the financial statements of Santa Cruz Metropolitan Transit District, taken as a whole. The accompanying schedule of expenditures of federal awards is 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 is not a required part of the financial statements. The accompanying statements of operating expenses by function are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

BROWN ARMSTRONG RANDALL
REYES PAULDEN & McCOWN
ACCOUNTANCY CORPORATION

A handwritten signature in black ink, appearing to read "R. Paulden", is written over the printed name of the firm.

Bakersfield, California
September 20, 2001

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
BALANCE SHEETS
JUNE 30, 2001 AND 2000**

	2001	2000
<u>ASSETS</u>		
CURRENT ASSETS		
Cash and cash equivalents	\$ 23,292,520	\$ 18,757,493
Grants and other receivables	3,954,517	3,398,558
Inventory	734,398	840,948
Prepays	18,452	126,249
Total Current Assets	27,999,887	23,123,248
RESTRICTED ASSETS		
Cash and cash equivalents	6,411,409	6,022,487
PROPERTY AND EQUIPMENT		
Buildings and improvements	10,081,614	10,050,818
Transportation vehicles	19,288,954	18,958,986
Operations equipment	1,252,569	1,175,929
Other equipment	1,195,528	1,091,094
Other vehicles	747,229	699,446
Office equipment	1,164,113	1,252,368
	33,730,007	33,228,641
Less: accumulated depreciation	(18,206,492)	(17,398,014)
	15,523,515	15,830,627
Construction in progress	1,018,441	111,073
Land	3,763,501	3,763,501
Property and Equipment, net	20,305,457	19,705,201
TOTAL ASSETS	\$ 54,716,753	\$ 48,850,936

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

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
BALANCE SHEETS (Continued)
JUNE 30, 2001 AND 2000**

	2001	2000
<u>LIABILITIES AND FUND EQUITY</u>		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 1,289,185	\$ 1,053,763
Accrued payroll and employee benefits	2,283,981	2,090,702
FEMA/OES settlement liabilities	-	354,725
Other accrued liabilities	3,346,179	2,382,664
Security deposit	14,764	10,364
Deferred revenue	527,339	61,039
Total Current Liabilities	7,461,448	5,953,257
LIABILITIES PAYABLE FROM RESTRICTED ASSETS		
Deferred revenue	6,411,409	6,022,487
LONG-TERM LIABILITIES		
Workers' compensation liabilities	2,869,840	1,543,000
Total Liabilities	16,742,697	13,518,744
FUND EQUITY		
Contributed capital		
Federal grants	8,856,579	8,511,272
State grants	6,417,677	6,270,126
Local grants	936,625	910,064
Other grants	14,184	21,532
Total Contributed Capital	16,225,065	15,712,994
Retained Earnings	21,748,991	19,619,198
Total Fund Equity	37,974,056	35,332,192
TOTAL LIABILITIES AND FUND EQUITY	\$ 54,716,753	\$ 48,850,936

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

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF REVENUES AND EXPENSES
FOR THE YEARS ENDED JUNE 30, 2001 AND 2000**

	<u>2001</u>	<u>2000</u>
OPERATING REVENUE		
Passenger fare	\$ 3,836,904	\$ 3,753,062
Special transit fare	1,630,576	1,559,392
Purchased transportation revenue	<u>443,492</u>	<u>341,585</u>
Total Operating Revenue	<u>5,910,972</u>	<u>5,654,039</u>
OPERATING EXPENSES		
Wages, salaries and employee benefits	20,345,599	16,577,939
Purchased transportation services	2,388,654	2,674,552
Material and supplies	2,498,448	2,121,313
Other expenses	3,167,313	3,174,515
Depreciation	<u>1,791,889</u>	<u>1,869,604</u>
Total Operating Expenses	<u>30,191,903</u>	<u>26,417,923</u>
Net Operating Loss	<u>(24,280,931)</u>	<u>(20,763,884)</u>
NONOPERATING REVENUES (EXPENSES)		
Sales and use tax	16,356,095✓	14,807,812✓
Transportation Development Act assistance	6,430,011	4,824,062
Section 8/5303 planning funds	-	34,963
Section 9/5307 operating assistance	505,614	505,614
Section 18/5307 operating assistance	39,697	36,918
Federal operating assistance grants	175,302	438,046
Other state operating assistance	-	63,993
Local transportation funds	35,295	28,152
Interest income	1,249,907	958,795
Rental income	146,350	113,282
Other revenue	184,539	243,406
Loss on disposal of inventory	(213,491)	-
Reversal of FEMA/OES contingencies	<u>-</u>	<u>3,076,147</u>
Total Nonoperating Revenues	<u>24,909,319</u>	<u>25,131,190</u>
NET INCOME	<u>\$ 628,388</u>	<u>\$ 4,367,306</u>

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

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF CHANGES IN FUND EQUITY
FOR THE YEARS ENDED JUNE 30, 2001 AND 2000**

	Contributed Capital				Retained Earnings	Total
	Federal	State	Local	Other		
Balance at June 30, 1999	\$ 8,788,166	\$ 5,513,965	\$ 860,148	\$ 46,200	\$ 13,759,962	\$ 28,968,441
Net income	-	-	-	-	4,367,306	4,367,306
Depreciation charged to contributed capital	(1,108,245)	(362,045)	(14,292)	(7,348)	1,491,930	-
Capital grant funds earned	<u>831,351</u>	<u>1,118,206</u>	<u>64,208</u>	<u>(17,320)</u>	<u>-</u>	<u>1,996,445</u>
Balance at June 30, 2000	8,511,272	6,270,126	910,064	21,532	19,619,198	35,332,192
Net income	-	-	-	-	628,388	628,388
Depreciation charged to contributed capital	(1,058,179)	(407,278)	(28,600)	(7,348)	1,501,405	-
Capital grant funds earned	1,464,179	555,381	55,161	-	-	2,074,721
Capital grant assets disposed (net)	<u>(60,693)</u>	<u>(552)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(61,245)</u>
Balance at June 30, 2001	<u>\$ 8,856,579</u>	<u>\$ 6,417,677</u>	<u>\$ 936,625</u>	<u>\$ 14,184</u>	<u>\$ 21,748,991</u>	<u>\$ 37,974,056</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, 2001 AND 2000**

	<u>2001</u>	<u>2000</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Operating loss	\$ (24,280,931)	\$ (20,763,884)
Adjustments to reconcile net operating loss to net cash used in operating activities:		
Advertising revenue	156,000	-
Depreciation	1,791,889	1,869,604
Loss on disposition of equipment	-	155,498
Changes in assets and liabilities:		
Receivables	(555,960)	248,751
Inventory	106,549	(19,297)
Prepaid expenses	107,797	(123,429)
Accounts payable	235,423	239,283
Other liabilities	<u>2,988,530</u>	<u>(383,269)</u>
Net Cash Used in Operating Activities	<u>(19,450,703)</u>	<u>(18,776,743)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Operating grants received, including sales and use tax	23,274,055	23,960,365
Other nonoperating	<u>760</u>	<u>(3,430,872)</u>
Net Cash Provided by Noncapital Financing Activities	<u>23,274,815</u>	<u>20,529,493</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of property and equipment	21,004	50,657
Construction in progress	(907,368)	-
Capital grants received	2,074,721	2,880,810
Capital assets acquired	<u>(1,484,778)</u>	<u>(1,933,245)</u>
Net Cash (Used in) Provided by Capital and Related Financing Activities	<u>(296,421)</u>	<u>998,222</u>
CASH FLOWS PROVIDED BY INVESTING ACTIVITIES		
Investment and rental income received	<u>1,396,257</u>	<u>1,067,974</u>
Net Increase in Cash and Cash Equivalents	4,923,948	3,818,946
Cash and Cash Equivalents at Beginning of Year	<u>24,779,981</u>	<u>20,961,035</u>
Cash and Cash Equivalents at End of Year	<u>\$ 29,703,929</u>	<u>\$ 24,779,981</u>

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

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2001 AND 2000**

NOTE 1 - OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Organization

The Santa Cruz Metropolitan Transit District (the District) 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, Capitola and the unincorporated areas of Santa Cruz County. The District is governed by a Board of eleven directors, and one Ex-Officio director representing the University of California, Santa Cruz. At June 30, 2001, the directors were as follows:

Chairperson:	Jan Beautz		
Vice Chair:	Emily Relly		
Members:	Sheryl Ainsworth	Bruce Gabriel	Christopher Krohn
	Jeff Almquist	Michelle Hinkle	Rafael Lopez
	Tim Fizmaurice	Mike Keogh	Dennis Norton
Ex-Officio:	Mike Rotkin		

B. Reporting Entity

The District and the Santa Cruz Civic Improvement Corporation (the Corporation) have a financial and operational relationship, which meets the reporting entity definition criteria of GASB Statement No. 14, *The Financial Reporting Entity*, for inclusion of the Corporation as a component unit of the District. Accordingly, the financial activities of the Corporation have been included in the financial statements of the District. For the years ending June 30, 2001 and 2000, this activity was 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 the District for the construction and acquisition of major capital facilities.

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

B. Reporting Entity (Continued)

The following are those aspects of the relationship between the District and the Corporation, which satisfy GASB Statement No. 14 criteria.

Accountability:

1. The Corporation's Board of Directors were appointed by the District's Board of Directors.
2. The District 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 the District.
 - The District exercises significant influence over operations of the Corporation as it is anticipated that the District will be the sole lessee of all facilities owned by the Corporation. Likewise, it is anticipated that the District'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 the District based upon the following:
 - The District has assumed a "moral obligation", and potentially a legal obligation, for any debt incurred by the Corporation.

C. Basis of Accounting

The District maintains its records on the accrual basis of accounting whereby revenues are recognized when earned and expenses are recognized when the related liability is incurred. The District follows all Governmental Accounting Standards Board (GASB) accounting standards and all applicable Financial Accounting Standards Board (FASB) accounting standards.

D. Cash and Cash Equivalents

The District considers all highly liquid investments with a maturity date within three months of the date acquired to be cash equivalents. The District deposits funds into an external investment pool maintained by the County of Santa Cruz. These deposits are considered cash equivalents. The County of Santa Cruz 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, banker's acceptances, repurchase agreements, and the State Treasurer's investment pool. Cash and cash equivalents are stated at fair value. For purposes of the statement of cash flows, the District considers all highly liquid investments (including restricted assets) to be cash equivalents.

E. Inventory

Inventory is carried at cost. Inventory held by the District consists of spare bus parts that are consumed by the District and are not for resale purposes.

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

F. Restricted Assets

The cash resulting from a settlement agreement as described in Note 8, represents proceeds restricted by the Federal Transit Administration. Restricted assets at June 30, are as follows:

	<u>2001</u>	<u>2000</u>
Cash and cash equivalents		
Settlement agreement with contractor	<u>\$ 6,411,409</u>	<u>\$ 6,022,487</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 structures	20-30 years
Revenue vehicles	12 years
Other vehicles and equipment	3-10 years

The District has completed and capitalized the Scotts Valley Transit Center in fiscal 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 the District's funding sources for this project and has retained an interest in the property. The title to the property is retained by both the District 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 the District's financial statements.

H. Sales and Use Tax

The District receives a .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, the District is allocated, through the Santa Cruz County Regional Transportation Commission, a portion of the .25% sales and use tax levied by the Transportation Development Act.

I. Capital Grants

Capital grants for the acquisition of property, buildings, and equipment are accrued as contributed capital as the related eligible expenditures are incurred. Depreciation on assets acquired with contributed capital is charged to contributed capital.

J. Operating Assistance Grants

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

K. Self-Insurance

The District is self-insured for the first \$100,000 of general and vehicular liability. For settlements in excess of \$100,000, the District has total coverage up to \$20,000,000 per occurrence. Additionally, the District is self insured up to \$350,000 for workers' compensation claims. The District has recorded a liability for estimated claims to be paid including incurred but not reported claims.

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

L. Employee Benefits

Vacation 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 District service.

M. Payroll

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

N. Pension Costs

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

O. 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 and 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.

P. Reclassifications

Certain accounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year financial statements. These reclassifications did not have any affect on fund equity.

NOTE 2 - CASH AND CASH EQUIVALENTS

Cash and cash equivalents consists of the following at June 30,:

	<u>2001</u>	<u>2000</u>
Cash on hand	\$ 27,612	\$ 21,485
Demand deposits	276,140	308,713
Deposits in Santa Cruz County Pooled Investment Fund	<u>29,400,177</u>	<u>24,449,783</u>
	<u>\$ 29,703,929</u>	<u>\$ 24,779,981</u>

Cash on Hand and Cash in Banks

Cash is maintained in a financial institution, which provides deposit protection on the bank balance from the Federal Deposit Insurance Corporation. Additionally, the California Government Code requires all financial institutions to maintain an investment pool equal to 110% of all government deposits held by the institution as collateral for such deposits.

Cash is categorized below to give an indication of the level of risk assumed by the District. Category 1 includes cash balances that are insured in the District's name. Category 2 includes cash balances for which the collateral securities are held by the financial institution in the District's name. Category 3 includes uninsured cash balance for which the collateral securities are held by the financial institution but not in the District's name.

NOTE 2 - CASH AND CASH EQUIVALENTS (Continued)

Cash on Hand and Cash in Banks

Cash at June 30, 2001 consists of the following:

	Balance per SCMTD	Balance per Bank	Categories		
			1	2	3
Cash in banks	\$ 276,140	\$ 642,794	\$ 100,000	\$ 542,794	\$ -
Cash on hand	<u>27,612</u>				
	<u>\$ 303,752</u>				

Cash at June 30, 2000 consists of the following:

	Balance per SCMTD	Balance per Bank	Categories		
			1	2	3
Cash in banks	\$ 308,713	\$ 123,510	\$ 100,000	\$ 23,510	\$ -
Cash on hand	<u>21,485</u>				
	<u>\$ 330,198</u>				

Investments

At June 30, 2001 and 2000, the District had \$29,400,177 and \$24,449,783, respectively, invested in the Santa Cruz County Pooled Investment Fund. Pooled cash held in the County Investment Fund is considered uncategorized. In accordance with GASB guidelines, the District has marked all investments to their market value.

NOTE 3 - RECEIVABLES

Receivables at June 30, are as follows:

	2001	2000
Federal grants	\$ 642,968	\$ 346,734
State grants	413,419	479,128
Local grants	25,297	20,619
Sales tax revenue	2,643,900	2,306,700
Other	<u>228,933</u>	<u>245,377</u>
	<u>\$ 3,954,517</u>	<u>\$ 3,398,558</u>

NOTE 4 - AVAILABLE NET ASSETS

An analysis of the District's available (undesignated) net assets at June 30, are as follows:

	<u>2001</u>	<u>2000</u>
Current assets	\$ 27,999,887	\$ 22,963,249
Current liabilities	<u>(7,461,448)</u>	<u>(5,793,257)</u>
Working capital	20,538,439	17,169,992
Less:		
Inventory	(734,398)	(840,948)
Prepaid expenses	<u>(18,452)</u>	<u>(126,249)</u>
Total available net assets	<u>19,785,589</u>	<u>16,202,795</u>
Net assets designated for the following:		
Cash flow	(2,600,000)	(2,600,000)
Workers' compensation reserve	(1,170,000)	(730,000)
Insurance reserve	(600,000)	(375,000)
Alternative fuel conversion fund	(462,000)	-
Bus stop improvements	(400,000)	(300,000)
Net assets required to fund transportation improvement program for fiscal years 2001-2006	<u>(13,997,795)</u>	<u>(10,000,000)</u>
Total designated net assets	<u>(19,229,795)</u>	<u>(14,005,000)</u>
Excess of available net assets over (under) designated net assets	<u>\$ 555,794</u>	<u>\$ 2,197,795</u>

NOTE 5 - CAPITAL GRANTS

The District receives grants from the Federal Transit Administration (FTA), which provides financing primarily for the acquisition of rolling stock. The District also receives grants under the State Transportation Development Act and State Toll Bridge revenue programs 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, are as follows:

	<u>2001</u>	<u>2000</u>
Federal grants	\$ 1,464,179	\$ 831,351
State grants	555,381	1,118,206
Transportation Development Act (local transportation grants)	<u>55,161</u>	<u>46,888</u>
Total Capital Assistance	<u>\$ 2,074,721</u>	<u>\$ 1,996,445</u>

NOTE 6 - COMMITMENTS

The District leases a number of its facilities under operation leases extending through 2006. For the years ended June 30, 2001 and 2000, rental expense relating to the leases was \$515,681 and \$484,245, respectively. The District also leases to others retail space in their transit facilities under noncancelable agreements. Minimum lease payments and receipts for existing operating leases are as follows:

<u>Year Ending June 30</u>	<u>Lease Commitments</u>	<u>Rent Income</u>	<u>Net</u>
2002	\$ 537,228	\$ 106,319	\$ 430,909
2003	518,837	100,435	418,402
2004	360,980	102,728	258,252
2005	346,030	73,077	272,953
2006	179,732	10,244	169,488
Thereafter	-	-	-
	<u>\$ 1,942,807</u>	<u>\$ 392,803</u>	<u>\$ 1,550,004</u>

NOTE 7 - JOINT VENTURES (Joint Powers Authority)

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

CalTIP arranges for and provides property and liability insurance for its 25 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 year ended April 30, 2001 is as follows:

Total assets	\$ 11,859,727
Total liabilities	<u>9,145,867</u>
Fund Balance	<u>\$ 2,713,860</u>
Total revenues	\$ 3,880,492
Total expenditures and cumulative effect of accounting change	<u>3,426,587</u>
Net Increase in Fund Balance	<u>\$ 453,905</u>

The District's share of year-end assets, liabilities, or fund balance has not been calculated by CalTIP.

NOTE 8 - WATSONVILLE FLEET MAINTENANCE FACILITY

The District'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.

In addition, due to design and construction deficiencies by the design and building contractors involved in the original project, the District 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 the District during fiscal year 1996, representing damages less attorney fees. The use of these proceeds, and the interest earned thereon, is restricted by the various governmental agencies that originally contributed the monies to build the fleet maintenance facility. Accordingly, the net restricted amount of \$6,411,409 and \$6,022,487 is reflected on the balance sheets as deferred revenue at June 30, 2001 and 2000, respectively. The District is currently working towards building a new facility in Santa Cruz.

NOTE 9 - CONTINGENCIES

The District 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, the District believes that any required reimbursement will not be material.

Additionally, the District 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 financial statements.

NOTE 10 - DEFINED BENEFIT PENSION PLAN

Plan Description

The District'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. The District selects optional benefit provisions from the benefit menu by contract with CalPERS and adopts those benefits through Board 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 317 active plan members in the Fund as of June 30, 2001 which are required to contribute a percent of their annual covered salary. In lieu of salary increases and for employees who agreed to salary reductions in certain prior years, the District agreed to pay a portion of the employee contribution, based on negotiated formulas. The District 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, 2001 was 0%. 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 fiscal year ended June 30, 2001, the District's annual pension cost of \$763,788 was equal to the District's required and actual contributions. This includes the District's contribution to the employee contribution requirement. The required contribution for fiscal year ended June 30, 2001 was determined as part of the June 30, 1998 actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 8.25% investment rate of return (net of administration expenses); (b) projected salary increases that vary by duration of service ranging from 3.75% to 14.21% for miscellaneous members, and (c) 3.75% cost-of-living adjustment. Both (a) and (b) include an inflation component of 3.50%. 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 excess assets are being amortized as a level percentage of projected payroll on a closed basis. The remaining amortization period at June 30, 2001 was 66 years.

Three-Year Trend Information for the Fund

Three-year trend information, with respect to the District's participation in CalPERS is as follows:

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/99	\$ 945,978	100%	\$ -
6/30/00	\$ 693,649	100%	\$ -
6/30/01	\$ 763,788	100%	\$ -

Required Supplementary Information

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

<u>Valuation Date</u>	<u>Entry Age Normal 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>
6/30/97	\$ 27,127,127	\$ 33,583,405	\$ (6,456,278)	123.8%	\$ 9,201,439	(70.166)%
6/30/98	29,651,308	41,065,136	(11,413,828)	138.5%	9,751,513	(117.047)%
6/30/99	32,467,163	47,476,596	(15,009,433)	146.2%	10,560,478	(142.128)%

NOTE 11 - POST-RETIREMENT BENEFITS

The District provides post-retirement benefits to its employees who have completed at least ten years of full-time service with the District, have reached the age of 50 and have retired under the provisions of CalPERS while an employee of the District. The District pays a portion of the premiums for medical insurance for retirees and eligible dependents. The District also provides dental, vision and life insurance plan coverage of retirees and eligible dependents until the retiree attains the age of 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. The costs of providing these benefits are recognized when paid. The District has recognized approximately \$365,747 and \$258,000 of expense for these benefits for the years ending June 30, 2001 and 2000, respectively.

NOTE 12 - DEFERRED COMPENSATION PLAN

The District 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 district 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. The District employees participate in two such plans, the Great-West Life and Annuity Insurance (Great-West) plan and the other through CalPERS.

At June 30, 2001, all amounts held under the Great-West plan and the CalPERS plan are held in trust and are not reflected on the accompanying balance sheet as required under Statement No. 27 of the Governmental Accounting Standards Board, *Accounting Standards for Pensions by State and Local Governmental Employers*.

NOTE 13 - RISK MANAGEMENT

The District 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 the District carries commercial insurance. The District 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 August 1, 2001. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of pay-outs and other economic and social factors. The IBNR amount based on the actuarial study was determined to be \$5,476,041 at June 30, 2001.

NOTE 14 - TRANSPORTATION DEVELOPMENT ACT/CALIFORNIA ADMINISTRATIVE CODE

The District is subject to compliance with the Transportation Development Act 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 State Transit Assistance Fund in an amount which exceeds the claimant's capital and operating costs, less the required fares, and local support. The District did not receive Transportation Development Act 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. The District did maintain its accounts and records in accordance with the Uniform System of Accounts and Records for Transit Operators.

Sections 99267 and 99268.1

Pursuant to the Transportation Development Act, the District is defined as an older operator and is not required to meet the fare box ratio requirement of the Act. The District has met the 50% expenditure limitation requirement.

NOTE 15 - NEW ACCOUNTING PRONOUNCEMENT

In June 1999, the Governmental Accounting Standards Board issued Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis for-State and Local Governments*. The requirements of the Statement become effective for the District for the year ending June 30, 2003. The new statement will require the basic financial statements to include Management's Discussion and Analysis (MD&A), government-wide financial statements, fund financial statements, notes to the financial statements and required supplementary information. Management has not yet determined the effect of adopting this statement on the District's financial statements.

SUPPLEMENTARY INFORMATION

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
STATEMENTS OF OPERATING EXPENSES
JUNE 30, 2001 AND 2000**

	<u>2001</u>	<u>2000</u>
Labor		
Operators' salaries and wages	\$ 5,284,468	\$ 4,859,665
Other salaries and wages	4,695,584	4,296,143
Overtime	1,198,745	1,070,853
Fringe Benefits		
Absence with pay	2,371,087	2,115,000
Pension plans	763,788	693,649
Vision, medical, and dental plans	2,445,495	2,068,450
Workers' compensation insurance	3,020,777	1,044,228
Disability insurance	464,841	329,170
Other fringe benefits	100,814	100,782
Services		
Accounting	196,961	61,415
Administrative and banking	170,483	172,210
Professional and technical services	642,822	935,306
Security	350,919	322,408
Outside repairs	391,863	318,002
Other services	168,591	166,092
Materials and Supplies Consumed		
Fuels and lubricants	1,169,459	915,027
Tires and tubes	148,666	152,440
Vehicle parts	655,379	576,473
Other materials and supplies	524,943	477,373
Utilities	263,937	265,263
Casualty and Liability Costs	213,149	207,096
Taxes and Licenses	37,044	33,934
Purchased Transportation Services		
Highway 17	-	412,827
Paratransit	2,388,654	2,261,725
Miscellaneous Expenses	194,153	191,974
Equipment and Facility Lease	537,392	500,814
Depreciation		
Property acquired with operator funds	290,484	377,674
Property acquired by federal, state or TDA funds	1,501,405	1,491,930
Total Operating Expenses	<u>\$ 30,191,903</u>	<u>\$ 26,417,923</u>

OTHER SCHEDULES AND REPORTS

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2001**

<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			
Preliminary Engineering	20.500*	CA-03-0413	\$ 168,695
Fare Boxes	20.500*	CA-03-0365	<u>51,025</u>
			<u>219,720</u>
Section 9/5307			
Fare Boxes	20.507*	CA-90-X625	16,660
Talking Bus - Capital	20.507*	CA-90-X625	3,983
MIS Hardware - Capital	20.507*	CA-90-X752	21,167
CMAQ Fare Boxes	20.507*	CA-90-X752	20,373
Fare Boxes	20.507*	CA-90-X691	3,857
Fare Boxes	20.507*	CA-90-X902	610,746
ADA Paratransit Vehicles	20.507*	CA-90-X902	226,408
Repower Buses	20.507*	CA-90-Y024	516,565
Operating Assistance	20.507*	CA-90-Y024	<u>505,614</u>
			<u>1,925,373</u>
Section 18/5311			
Operating Assistance	20.509	649068	<u>39,697</u>
Total Expenditures of Federal Awards			<u>\$ 2,184,790</u>

* Major federal financial assistance program.

See accompanying notes to schedule of federal financial assistance.

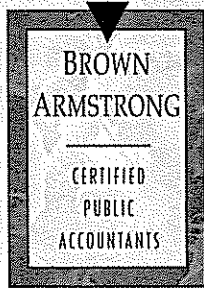
**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2001**

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 (the District). 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.



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Vonie L. Chroman, CPA
Michelle L. Gonzales, CPA
Amanda E. Wilson, CPA

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS AND THE RULES AND
REGULATIONS OF THE TRANSPORTATION DEVELOPMENT ACT**

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

We have audited the financial statements of Santa Cruz Metropolitan Transit District as of and for the year ended June 30, 2001, and have issued our report thereon dated September 20, 2001. 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 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. 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 *Government Auditing Standards*.

Internal Control Over Financial Reporting

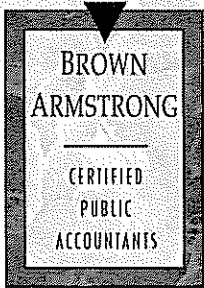
In planning and performing our audit, we considered Santa Cruz Metropolitan Transit District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of management, the Board of Directors, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

BROWN ARMSTRONG RANDALL
REYES PAULDEN & McCOWN
ACCOUNTANCY CORPORATION

A handwritten signature in black ink, appearing to read "B. Paulden", written in a cursive style.

Bakersfield, California
September 20, 2001



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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

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

- Lynn R. Krausse, CPA, MST
Chris M. Thornburgh, CPA
Joan M. Anderson, CPA
Bradley M. Hankins, CPA
B. Marie Ebersbacher, CPA, CFE
Eric Xin, CPA
Melinda A. McDaniel, CPA
Thomas M. Young, CPA
Vonie L. Chroman, CPA
Michelle L. Gonzales, CPA
Amanda E. Wilson, CPA

Compliance

We have audited the compliance of Santa Cruz Metropolitan Transit District with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended June 30, 2001. Santa Cruz Metropolitan Transit District's major federal program is 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 its major federal program is the responsibility of Santa Cruz Metropolitan Transit District's management. Our responsibility is to express an opinion on 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 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 on 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 are applicable to its major federal programs for the year ended June 30, 2001.

Internal Control Over Compliance

The management of 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 Santa Cruz Metropolitan Transit District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order 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.

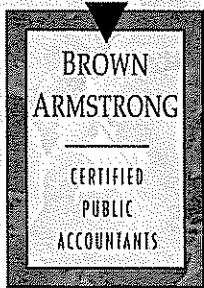
Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended for the information of management, the Board of Directors, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

BROWN ARMSTRONG RANDALL
REYES PAULDEN & McCOWN
ACCOUNTANCY CORPORATION

A handwritten signature in black ink, appearing to read "R. Paulden", is written over the printed name of the firm.

Bakersfield, California
September 20, 2001



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**REPORT ON COMPLIANCE WITH THE
TRANSPORTATION DEVELOPMENT ACT**

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 (the District), as of and for the year ended June 30, 2001, and have issued our report there on dated September 20, 2001.

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.

Compliance with laws, regulations, contracts and grants applicable to the District is the responsibility of the management of the District. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the District's compliance with certain provisions of the Transportation Development Act, including Public Utilities Code Section 99245 as enacted and amended by statute through June 30, 2001, and the allocation instructions and resolutions of the Santa Cruz County Regional Transportation Commission as required by Section 6667 of the California Code of Regulations. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests indicated that, with respect to the items tested, the District complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the District had not complied, in all material respects, with those provisions.

This report is intended for the information of management, the Board of Directors, the State Controller's Office, the U.S. Department of Transportation, and officials of applicable grantor agencies. However, this report is a matter of public record and its distribution is not limited.

**BROWN ARMSTRONG RANDALL
REYES PAULDEN & McCOWN
ACCOUNTANCY CORPORATION**

Bakersfield, California
September 20, 2001

FINDINGS AND QUESTIONED COSTS SECTION

**SANTA CRUZ METROPOLITAN TRANSIT DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
JUNE 30, 2001**

I. Summary of Auditor's Results

Financial Statements

Type of auditors' report issued:

Unqualified

Internal control over financial reporting:

Material weakness identified?

— Yes No

Reportable conditions identified that are not considered to be material weaknesses?

— Yes None reported

Noncompliance material to financial statements noted?

— Yes No

Federal Awards

Internal control over major federal programs:

Material weakness identified?

— Yes No

Reportable conditions identified that are not considered to be material weaknesses?

— Yes None reported

Type of auditors' report issued on compliance for major programs:

Unqualified

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?

— Yes No

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Clusters

20.500

Federal Transit Administration-Section 3

20.507

Federal Transit Administration-Section 9

Dollar threshold used to distinguish Type A & B programs:

\$300,000

Auditee qualified as low risk auditee?

— Yes No

II. Findings Relating to Financial Statements Required Under GAGAS

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, 2000) Findings and Current Year Status Follows

Finding 2000-1

Equipment and Real Property Management

The District is required to perform a physical count of their fixed assets every two years as required by federal regulations. The District did not perform a physical count in prior year (fiscal year ending June 30, 1999) and did not fully complete (note: they have started but have not completed the count as of June 30, 2000 and as of the end of field work) the physical count in the current year.

Recommendation

As required by federal regulations, we recommend that the District complete a fixed asset count every two years.

Current Year Status

Implemented.