

***CITY OF SOMERVILLE, MASSACHUSETTS***

***REPORT ON EXAMINATION OF  
BASIC FINANCIAL STATEMENTS***

***FISCAL YEAR ENDED JUNE 30, 2006***

CITY OF SOMERVILLE, MASSACHUSETTS

REPORT ON EXAMINATION OF BASIC FINANCIAL STATEMENTS

JUNE 30, 2006

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## Independent Auditors' Report

To the Honorable Mayor and Board of Aldermen  
City of Somerville, Massachusetts

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Somerville, Massachusetts, as of and for the fiscal year ended June 30, 2006 (except for the Somerville Contributory Retirement System which is as of and for the year ended December 31, 2005), which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Somerville, Massachusetts' management. Our responsibility is to express opinions on these financial statements based on our audit.

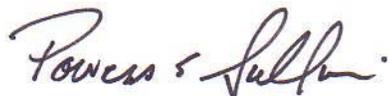
We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and 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 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 respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Somerville, Massachusetts, as of June 30, 2006 (except for the Somerville Contributory Retirement System which is as of December 31, 2005), and the respective changes in financial position and cash flows, where applicable, thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As more fully described in Note 1, the City has restated the beginning fund balance position and net assets to recognize its water and sewer operations as proprietary funds.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 22, 2007, on our consideration of the City of Somerville, Massachusetts' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants 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 read in conjunction with this report in considering the results of our audit.

Management's discussion and analysis, located on pages 3 through 11, and the schedule of revenues, expenditures and changes in fund balance – general fund – budget and actual, located after the notes to the basic financial statements, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in dark ink, appearing to read "Powers & Sullivan". The signature is written in a cursive, flowing style.

January 22, 2007

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# ***Management's Discussion and Analysis***

## ***Management's Discussion and Analysis***

As management of the City of Somerville, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City of Somerville for the fiscal year ended June 30, 2006. We encourage readers to consider the information presented in this report.

### ***Overview of the Financial Statements***

This discussion and analysis is intended to serve as an introduction to the City of Somerville's basic financial statements. The City of Somerville's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The approach focuses on both the City as a whole (government-wide) and the fund financial statements. The government-wide financial statements provide both long-term and short-term information about the City as a whole. The fund financial statements focus on the individual parts of the City government, reporting the City's operations in more detail than the government-wide statements. Both presentations (government-wide and fund) allow the user to address relevant questions, broaden the basis of comparison and enhance the City's accountability. An additional part of the basic financial statements are the notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

**Government-wide financial statements.** The *government-wide financial statements* are designed to provide readers with a broad overview of the City of Somerville's finances, in a manner similar to a private-sector business. The statements provide both short-term and long-term information about the City's financial position, which assists in assessing the City's economic position at the end of the fiscal year. The statements are prepared using the full accrual basis of accounting. All revenues and expenses connected with the fiscal year are considered even if the cash involved has not been received or disbursed. The government-wide financial statements include two statements:

The *statement of net assets* presents information on all of the City of Somerville's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City of Somerville is improving or deteriorating. The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of Somerville that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City of Somerville include general government, public safety, highways and streets, public works and cemetery, education, health and human services, employee benefits and capital, water and sewer, and culture and recreation.

**Fund financial statements** - A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Somerville, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City of Somerville can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

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

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City of Somerville maintains fifteen individual governmental funds. Information is presented separately for the general fund and the community development fund in the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances. Data for certain governmental funds are combined into a single aggregated presentation under the caption *nonmajor governmental funds*.

The City of Somerville adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided as required supplementary information for the general fund to demonstrate compliance with this budget.

**Proprietary funds.** Proprietary funds provide the same information shown as business-type activities in the government wide financial statements, only in more detail. The City uses proprietary funds to account for its sewer and water operations.

**Fiduciary funds.** Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are *not* all reflected in the government-wide financial statement because the resources of those funds are *not* available to support the City of Somerville's own programs. The accounting used for fiduciary funds records transactions using the flow of economic resources measurement focus and the accrual basis of accounting.

The fiduciary fund financial statements provide separate information for the pension trust fund of the City and the private purpose trust funds of the City. All other fiduciary funds are combined into a single, aggregate presentation in the fiduciary fund financial statements under the caption agency funds.

**Notes to the financial statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

**Other information.** In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City of Somerville's budgetary basis of accounting. Required supplementary information can be found after the notes to the financial statements.

### ***Government-wide Financial Analysis***

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City of Somerville, Governmental assets exceeded liabilities by \$148.4 million and the business-type assets exceeded liabilities by \$10.2 million at the close of the most recent fiscal year. Key components of the City's activities are presented on the following pages.

			FY 2006	FY 2005
<b>Assets:</b>				
	Current assets.....	\$	75,679,014	\$ 71,521,507
	Noncurrent assets (excluding capital).....		36,000,117	34,163,553
	Capital assets.....		128,184,063	121,826,629
	<b>Total assets.....</b>		<b>239,863,194</b>	<b>227,511,689</b>
<b>Liabilities:</b>				
	Current liabilities (excluding debt).....		7,742,371	10,151,045
	Noncurrent liabilities (excluding debt).....		3,647,700	3,778,200
	Current debt.....		11,446,986	10,762,180
	Noncurrent debt.....		68,568,873	61,537,807
	<b>Total liabilities.....</b>		<b>91,405,930</b>	<b>86,229,232</b>
<b>Net Assets:</b>				
	Capital assets net of related debt.....		87,930,204	84,887,642
	Restricted.....		23,512,466	23,076,486
	Unrestricted.....		37,014,594	35,434,352
	<b>Total net assets.....</b>	\$	<b>148,457,264</b>	\$ <b>143,398,480</b>

The largest portion of the City of Somerville's net assets (59 percent) reflects its investment in capital assets (e.g., land, buildings, machinery, and equipment) less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to its citizens; consequently, these assets are *not* available for future spending. Although the City of Somerville's investment in its capital assets is reported net of related debt, it should be noted that resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the City of Somerville's net assets (16 percent) represents resources that are subject to external restrictions on how they may be used. These include funds for street improvement (Ch 90), community development, Section 108 loans, expendable and nonexpendable funds and school grants.

The remaining balance of unrestricted net assets \$37 million (25 percent) may be used to meet the government's ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the City of Somerville is able to report positive balances in its three categories of net assets, both for the government as a whole and for its separate governmental and business-type activities.

Included within the noncurrent assets (excluding capital) is \$35.4 million in future school construction reimbursement grants.

Long term liabilities include \$68.5 million in general obligation bonds and intergovernmental loans; \$2.4 million in compensated absence liabilities for unused vacation, special leave, and enhanced longevity benefits payable; and \$1.2 million in future year workers' compensation benefits payable.

**Governmental activities.** Governmental activities increased the City of Somerville's net assets by \$7.4 million.

	<b>FY 2006</b>	<b>FY 2005</b>
<b>Program revenues:</b>		
Charges for services.....	\$ 15,932,027	\$ 14,619,377
Operating grants and contributions.....	55,394,872	54,784,342
Capital grants and contributions.....	3,879,094	-
<b>General Revenues:</b>		
Real estate and personal property taxes.....	75,140,486	73,459,378
Tax liens.....	3,000,902	19,413
Motor vehicle and other excise taxes.....	5,189,010	5,429,328
Penalties and interest on taxes.....	619,375	599,400
Payments in lieu of taxes.....	354,342	341,819
Nonrestricted grants and contributions.....	28,456,720	28,411,388
Unrestricted investment income.....	1,476,584	929,090
Gain on sale of capital assets.....	150,484	867,752
Loss on disposal of capital assets.....	(2,148,301)	-
Other revenues.....	1,048,792	177,997
<b>Total revenues.....</b>	<b><u>188,494,387</u></b>	<b><u>179,639,284</u></b>
<b>Expenses:</b>		
General government.....	17,625,708	17,020,080
Public safety.....	39,481,659	38,887,851
Education.....	91,176,638	82,130,505
Public works.....	20,814,103	21,784,837
Intergovernmental subsidy.....	220,000	220,000
Community development.....	5,173,783	5,419,101
Human services.....	26,210	22,781
Culture and recreation.....	4,513,673	3,617,495
Interest.....	2,885,144	3,495,985
<b>Total expenses.....</b>	<b><u>181,916,918</u></b>	<b><u>172,598,635</u></b>
<b>Transfers.....</b>	<b><u>829,217</u></b>	<b><u>-</u></b>
<b>Change in net assets.....</b>	<b><u>\$ 7,406,686</u></b>	<b><u>\$ 7,040,649</u></b>

**Key elements of this increase are as follows:**

- Collections of licenses and permits increased \$600 thousand.
- An increase in investment income of \$550 thousand and strong tax lien activity of \$3.0 million were other one-time monies received by the City in fiscal 2006.
- Property taxes increased by \$1.7 million (2.3 percent) during the year. Most of this increase is the product of a restricted tax levy that totaled \$78.5 million.
- Operating grants for governmental activities increased by \$610 thousand million, mostly as a result of an increase in Education related grant proceeds.
- Capital grants Increased by \$3.8 million due to the increase in spending related to reimbursable school construction costs from the MSBA.

For the most part, expenses decreased in anticipation of revenue reductions. Noteworthy exceptions, however, were the City's costs for pensions and public works, which increased \$800 thousand (7.7%) and \$3 million (11.4%), respectively.

## Business-type Activities

This is the first year the City has elected to present the water and sewer operations as business-type activities. Relevant details to their operations are shown below.

	FY 2006	FY 2005
<b>Assets:</b>		
Current assets.....	\$ <u>10,256,313</u>	\$ <u>5,622,002</u>
<b>Liabilities:</b>		
Current liabilities (excluding debt).....	\$ <u>18,665</u>	\$ <u>944,994</u>
<b>Net Assets:</b>		
Unrestricted.....	\$ <u><u>10,237,648</u></u>	\$ <u><u>4,677,008</u></u>
	FY 2006	FY 2005
<b>Program revenues:</b>		
Charges for services.....	\$ 23,311,329	\$ 19,870,735
<b>General Revenues:</b>		
Tax liens.....	904,658	-
Unrestricted investment income.....	<u>201,498</u>	<u>25,366</u>
<b>Total revenues.....</b>	<b><u>24,417,485</u></b>	<b><u>19,896,101</u></b>
<b>Expenses:</b>		
Water.....	6,524,762	6,199,800
Sewer.....	<u>11,502,866</u>	<u>10,929,973</u>
<b>Total expenses.....</b>	<b><u>18,027,628</u></b>	<b><u>17,129,773</u></b>
<b>Transfers.....</b>	<b><u>(829,217)</u></b>	<b><u>-</u></b>
<b>Change in net assets.....</b>	<b><u><u>\$ 5,560,640</u></u></b>	<b><u><u>\$ 2,766,328</u></u></b>

The water enterprise fund realized net income of approximately \$1,689,000 from operations before transfers, contributions and non-operating items. This is due to the funds ability to set rates to cover costs of operations and recording receivables under the full accrual basis of accounting.

The sewer enterprise fund realized net income of approximately \$4,700,000 from operations before transfers, contributions, and non-operating items. This is due to the funds ability to set rates to cover costs of operations and recording receivables under the full accrual basis of accounting. Also there was approximately \$493,000 of sewer liens collected during fiscal year 2006.

### Financial Analysis of the Government's Funds

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

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

As of the end of the current fiscal year, the City of Somerville's governmental funds reported combined ending balances of \$45.7 million, an increase of \$8.7 million in comparison with the prior year. Approximately 37% of this total amount (\$16.9 million) constitutes *general fund unreserved fund balance*, which is available for spending at the government's discretion when certified as *free cash* by the Massachusetts Department of Revenue. Approximately 17.4% (\$7.9 million) of fund balance is also *unreserved* and reported in the special revenue, capital projects and permanent funds. The remainder is *reserved* to indicate that it is not available for new spending because it has already been 1) committed to liquidate prior period purchase orders and contracts, or pay ongoing capital articles (\$1.4 million) or 2) is restricted for expenditure by grants or other outside restrictions (\$19.4 million).

The general fund is the chief operating fund of the City of Somerville. At the end of the current fiscal year, unreserved fund balance of the general fund was \$16.9 million while the total fund balance equaled \$25.8 million. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 10.5 percent of total general fund expenditures, while total fund balance represents 16.1 percent of that same amount.

The City's general fund increased \$2.7 million during the current fiscal year. Key factors in this growth were a \$4.3 million increase in property tax revenues, an increase in parking fees of \$1.1 million, and debt service subsidies received from the water and sewer enterprise funds of approximately \$910,000. These individual increases were offset by a \$4.2 million increase in expenditures related to employee health care benefits.

### ***General Fund Budgetary Highlights***

The net change between the original budget and the final amended budget was a decrease of approximately (\$45,000). However, there occurred numerous transfers and reversions of prior encumbrances that can be briefly summarized as follows:

- \$2.4 million decrease in general government
- \$525 thousand increase in culture and recreation
- \$438 thousand increase in public works
- \$551 thousand increase in public safety
- \$1.1 million increase in public works
- \$300 thousand increase in transfers out

### ***Capital Asset and Debt Administration***

**Capital assets.** The City of Somerville's investment in capital assets for its governmental activities as of June 30, 2006, amounts to \$128.1 million (net of accumulated depreciation). This investment in capital assets includes land, buildings, system improvements, machinery and equipment, park facilities, roads, highways, and bridges. The net increase in the City's investment in capital assets for the current year was \$6.3 million. Additional information on the City's capital assets may be found in Note 4 to the financial statements.

	<b>2006</b>	<b>2005</b>
Land and land improvements.....	\$ 22,926,078	\$ 19,022,469
Construction in progress.....	5,674,956	1,102,642
Books and periodicals.....	774,743	828,668
Buildings and improvements.....	76,054,839	81,099,715
Machinery and equipment.....	1,473,107	1,600,407
Vehicles.....	2,124,077	1,769,392
Infrastructure.....	<u>19,156,263</u>	<u>16,403,336</u>
Total.....	<u>\$ 128,184,063</u>	<u>\$ 121,826,629</u>

Major capital asset events during the current fiscal year included the following:

- Various investments were made to improve and expand the buildings of the School department;
- A variety of infrastructure investments occurred within the street, water and sewer systems;
- Various departmental vehicle and equipment acquisitions;

In conjunction with the operating budget, the City annually prepares a capital budget for the upcoming fiscal year and a five-year Capital Improvement Plan (CIP) that is used as a guide for future capital expenditures.

**Long-term debt.** At the end of the current fiscal year, the City of Somerville had total bonded debt outstanding of \$73.9 million. Additionally, short-term borrowing is at \$6 million and is due to various school projects, building renovations and sewer projects.

#### **General Obligation Bonds Outstanding**

	<b>2006</b>	<b>2005</b>
Municipal Purpose April 1, 1998.....	\$ 12,950,000	\$ 13,905,000
Municipal Purpose February 15, 1997.....	13,155,000	14,105,000
Water Projects - July 1, 1996.....	-	110,000
Sewer Projects - July 1, 1996.....	-	115,000
MWRA Notes.....	6,135,860	4,022,987
Municipal Purpose February 15, 2002.....	22,480,000	23,650,000
General Obligation Bond March 15, 2004.....	9,449,999	10,230,000
Municipal Purpose - August 15, 2006.....	<u>7,440,000</u>	<u>-</u>
Total bonds and notes payable.....	71,610,859	66,137,987
Sections 108 Intergovernmental Loans.....	<u>2,340,000</u>	<u>2,620,000</u>
Total.....	<u>\$ 73,950,859</u>	<u>\$ 68,757,987</u>

The City's long-term debt increased by \$5.2 million during the fiscal year. This increase is the net effect of the pay down of debt and the issuance of \$2.6 million in MWRA bonds and \$7.4 million in municipal bonds.

Moody's Investors Service, Inc. and Standard & Poor's Corporation have assigned ratings of A1 and A+ to the City's bonds.

### ***Economic Factors and Next Year's Budgets and Rates***

- According to the U.S. Census Bureau, the median family income for the City in 2000 was \$51,243 compared with \$61,644 for the Commonwealth and \$49,600 for the nation. The per capita income was \$23,628, compared with \$25,952 for the Commonwealth and \$21,690 for the nation
- The unemployment rate for the City of Somerville is approximately 3.2 percent, which is a .3% increase from a rate of 2.9 percent a year ago. This compares favorably to the state's average unemployment rate of 4.9 percent and the national average of 4.9 percent.
- According to the City's Board of Assessors, the average 2005 single family home in the City is valued at \$412,400; the average two-family home is valued at \$507,400; the average 2005 commercial and industrial property is valued at \$1,093,700 – all compare favorably with state and national property values.

### ***Requests for Information***

This financial report is designed to provide a general overview of the City of Somerville's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Finance, City Hall, 93 Highland Ave, Somerville, Massachusetts 02143.

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# ***Basic Financial Statements***

**STATEMENT OF NET ASSETS**

JUNE 30, 2006

	<i>Primary Government</i>		
	Governmental Activities	Business-type Activities	Total
<b>ASSETS</b>			
<b>CURRENT:</b>			
Cash and short-term investments.....	\$ 47,046,622	\$ 826,630	\$ 47,873,252
Receivables, net of allowance for uncollectibles:			
Tax liens and foreclosures.....	3,037,215	70,729	3,107,944
Motor vehicle excise tax.....	505,868	-	505,868
User fees.....	-	9,357,805	9,357,805
Departmental and other.....	1,991,171	-	1,991,171
Intergovernmental.....	14,658,223	-	14,658,223
Loans.....	8,328,809	-	8,328,809
Other assets.....	670	1,149	1,819
Deferred charges on refunding.....	110,436	-	110,436
<b>NONCURRENT:</b>			
Receivables, net of allowance for uncollectibles:			
Intergovernmental.....	35,490,000	-	35,490,000
Deferred charges on refunding.....	510,117	-	510,117
Capital assets, net of accumulated depreciation.....	128,184,063	-	128,184,063
<b>TOTAL ASSETS.....</b>	<b>239,863,194</b>	<b>10,256,313</b>	<b>250,119,507</b>
<b>LIABILITIES</b>			
<b>CURRENT:</b>			
Warrants payable.....	1,905,024	-	1,905,024
Accrued payroll.....	1,189,505	18,665	1,208,170
Health claims payable.....	1,451,000	-	1,451,000
Tax refunds payable.....	755,940	-	755,940
Accrued interest.....	939,241	-	939,241
Payroll withholdings.....	289,959	-	289,959
Abandoned property.....	745,283	-	745,283
Deferred revenue.....	61,119	-	61,119
Compensated absences.....	267,900	-	267,900
Workers' compensation.....	137,400	-	137,400
Intergovernmental loans payable.....	280,000	-	280,000
Bonds and notes payable.....	11,166,986	-	11,166,986
<b>NONCURRENT:</b>			
Compensated absences.....	2,411,100	-	2,411,100
Workers' compensation.....	1,236,600	-	1,236,600
Intergovernmental loans payable.....	2,060,000	-	2,060,000
Bonds and notes payable.....	66,508,873	-	66,508,873
<b>TOTAL LIABILITIES.....</b>	<b>91,405,930</b>	<b>18,665</b>	<b>91,424,595</b>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt.....	87,930,204	-	87,930,204
Restricted for:			
Streets.....	1,772,765	-	1,772,765
Community development.....	8,662,523	-	8,662,523
Loans.....	8,328,809	-	8,328,809
Permanent funds:			
Expendable.....	177,763	-	177,763
Nonexpendable.....	433,126	-	433,126
Other specific purposes.....	4,137,480	-	4,137,480
Unrestricted.....	37,014,594	10,237,648	47,252,242
<b>TOTAL NET ASSETS.....</b>	<b>\$ 148,457,264</b>	<b>\$ 10,237,648</b>	<b>\$ 158,694,912</b>

See notes to basic financial statements.

**STATEMENT OF ACTIVITIES**

FISCAL YEAR ENDED JUNE 30, 2006

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
<b>Primary Government:</b>					
<i>Governmental Activities:</i>					
General government.....	\$ 17,625,708	\$ 2,498,254	\$ 1,259,517	\$ -	\$ (13,867,937)
Public safety.....	39,481,659	10,127,903	2,141,506	-	(27,212,250)
Education.....	91,176,638	2,130,300	42,363,167	3,879,094	(42,804,077)
Public works.....	20,814,103	375,219	1,764,836	-	(18,674,048)
Intergovernmental subsidy.....	220,000	-	-	-	(220,000)
Community development.....	5,173,783	500	5,466,570	-	293,287
Human services.....	26,210	537,723	54,178	-	565,691
Culture and recreation.....	4,513,673	262,128	426,816	-	(3,824,729)
Interest.....	2,885,144	-	1,918,282	-	(966,862)
<b>Total Governmental Activities.....</b>	<b>181,916,918</b>	<b>15,932,027</b>	<b>55,394,872</b>	<b>3,879,094</b>	<b>(106,710,925)</b>
<i>Business-Type Activities:</i>					
Water .....	6,524,762	7,760,415	-	-	1,235,653
Sewer.....	11,502,866	15,550,914	-	-	4,048,048
<b>Total Business-Type Activities.....</b>	<b>18,027,628</b>	<b>23,311,329</b>	<b>-</b>	<b>-</b>	<b>5,283,701</b>
<b>Total Primary Government.....</b>	<b>\$ 199,944,546</b>	<b>\$ 39,243,356</b>	<b>\$ 55,394,872</b>	<b>\$ 3,879,094</b>	<b>\$ (101,427,224)</b>

See notes to basic financial statements.

(Continued)

**STATEMENT OF ACTIVITIES (Continued)**

FISCAL YEAR ENDED JUNE 30, 2006

	<b>Primary Government</b>		
	Governmental Activities	Business-Type Activities	Total
<b>Changes in net assets:</b>			
Net (expense) revenue from previous page.....	\$ (106,710,925)	\$ 5,283,701	\$ (101,427,224)
<i>General revenues:</i>			
Real estate and personal property taxes, net of tax refunds payable.....	75,140,486	-	75,140,486
Tax and utility liens.....	3,000,902	904,658	3,905,560
Motor vehicle and other excise taxes.....	5,189,010	-	5,189,010
Penalties and interest on taxes.....	619,375	-	619,375
Payments in lieu of taxes.....	354,342	-	354,342
Grants and contributions not restricted to specific programs.....	28,456,720	-	28,456,720
Unrestricted investment income.....	1,476,584	201,498	1,678,082
Gain on sale of assets.....	150,484	-	150,484
Loss on disposal of capital assets.....	(2,148,301)	-	(2,148,301)
Miscellaneous.....	1,048,792	-	1,048,792
<i>Transfers, net</i> .....	829,217	(829,217)	-
Total general revenues and transfers.....	114,117,611	276,939	114,394,550
Change in net assets.....	7,406,686	5,560,640	12,967,326
<i>Net Assets:</i>			
Beginning of year (as restated).....	141,050,578	4,677,008	145,727,586
End of year.....	\$ 148,457,264	\$ 10,237,648	\$ 158,694,912

(Concluded)

**GOVERNMENTAL FUNDS  
BALANCE SHEET**

JUNE 30, 2006

<b>ASSETS</b>	General	Community Development	Nonmajor Governmental Funds	Total Governmental Funds
Cash and short-term investments.....	\$ 31,523,234	\$ 315,939	\$ 15,207,449	\$ 47,046,622
Receivables, net of uncollectibles:				
Tax liens and foreclosures.....	3,037,215	-	-	3,037,215
Motor vehicle excise taxes.....	505,868	-	-	505,868
Departmental and other.....	1,991,171	-	-	1,991,171
Intergovernmental.....	37,422,000	8,714,930	4,011,293	50,148,223
Loans.....	-	8,328,809	-	8,328,809
Other assets.....	670	-	-	670
<b>TOTAL ASSETS.....</b>	<b>\$ 74,480,158</b>	<b>\$ 17,359,678</b>	<b>\$ 19,218,742</b>	<b>\$ 111,058,578</b>
<b>LIABILITIES AND FUND BALANCES</b>				
<b>LIABILITIES:</b>				
Warrants payable.....	\$ 1,902,073	\$ -	\$ 2,951	\$ 1,905,024
Accrued payroll.....	965,715	21,798	201,992	1,189,505
Health claims payable.....	1,451,000	-	-	1,451,000
Tax refunds payable.....	755,940	-	-	755,940
Accrued interest on short-term debt.....	26,316	-	-	26,316
Payroll withholdings.....	287,009	-	2,950	289,959
Abandoned property.....	745,283	-	-	745,283
Deferred revenues.....	42,475,527	8,662,523	1,772,765	52,910,815
Notes payable.....	-	-	6,065,000	6,065,000
<b>TOTAL LIABILITIES.....</b>	<b>48,608,863</b>	<b>8,684,321</b>	<b>8,045,658</b>	<b>65,338,842</b>
<b>FUND BALANCES:</b>				
Reserved for:				
Encumbrances and continuing appropriations.....	1,407,479	-	-	1,407,479
Loans.....	-	8,328,809	-	8,328,809
Employee benefits.....	7,600,023	-	-	7,600,023
Perpetual permanent funds.....	-	-	433,126	433,126
Other specific purposes.....	-	-	3,103,659	3,103,659
Unreserved:				
Designated for subsequent year's expenditures.....	3,000,000	-	-	3,000,000
Undesignated, reported in:				
General fund.....	13,863,793	-	-	13,863,793
Special revenue funds.....	-	346,548	6,960,057	7,306,605
Capital projects funds.....	-	-	498,479	498,479
Permanent funds.....	-	-	177,763	177,763
<b>TOTAL FUND BALANCES.....</b>	<b>25,871,295</b>	<b>8,675,357</b>	<b>11,173,084</b>	<b>45,719,736</b>
<b>TOTAL LIABILITIES AND FUND BALANCES.....</b>	<b>\$ 74,480,158</b>	<b>\$ 17,359,678</b>	<b>\$ 19,218,742</b>	<b>\$ 111,058,578</b>

See notes to basic financial statements.

**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET  
TOTAL FUND BALANCES TO THE STATEMENT OF NET ASSETS**

FISCAL YEAR ENDED JUNE 30, 2006

Total governmental fund balances.....		\$ 45,719,736
Capital assets (net) used in governmental activities are not financial resources and, therefore, are not reported in the funds.....		128,184,063
Accounts receivable are not available to pay for current-period expenditures and, therefore, are deferred in the funds.....		52,849,696
In the statement of activities, interest is accrued on outstanding long-term debt, whereas in governmental funds interest is not reported until due.....		(912,925)
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds:		
Bonds and notes payable.....	(73,950,859)	
Workers compensation.....	(1,374,000)	
Compensated absences.....	<u>(2,679,000)</u>	
Net effect of reporting long-term liabilities.....		<u>(78,003,859)</u>
In the statement of activities, deferred losses are reported for refundings of debt, which are amortized over the shorter of the remaining life of the refunding bonds or refunded bonds. In governmental funds, defeasances of debt are expensed when the refunding bonds are issued.....		<u>620,553</u>
Net assets of governmental activities.....		<u>\$ 148,457,264</u>

See notes to basic financial statements.

**GOVERNMENTAL FUNDS**  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

FISCAL YEAR ENDED JUNE 30, 2006

	General	Community Development	Nonmajor Governmental Funds	Total Governmental Funds
<b>REVENUES:</b>				
Real estate and personal property taxes, net of tax refunds.....	\$ 76,923,448	\$ -	\$ -	\$ 76,923,448
Tax liens.....	986,111	-	-	986,111
Motor vehicle and other excise taxes.....	5,272,658	-	-	5,272,658
Payments in lieu of taxes.....	354,342	-	-	354,342
Intergovernmental.....	62,733,635	5,737,822	15,760,081	84,231,538
Departmental and other.....	14,418,864	-	5,318,575	19,737,439
Contributions.....	-	-	1,958	1,958
Investment income.....	1,057,635	41,146	333,839	1,432,620
Miscellaneous.....	-	-	1,750	1,750
<b>TOTAL REVENUES.....</b>	<b>161,746,693</b>	<b>5,778,968</b>	<b>21,416,203</b>	<b>188,941,864</b>
<b>EXPENDITURES:</b>				
Current:				
General government.....	9,063,439	-	726,547	9,789,986
Public safety.....	25,494,912	-	3,158,117	28,653,029
Education.....	44,937,889	-	18,484,404	63,422,293
Public works.....	17,896,777	-	2,290,660	20,187,437
Intergovernmental subsidy.....	-	220,000	-	220,000
Community development.....	-	4,846,091	324,692	5,170,783
Human services.....	-	-	6,339	6,339
Culture and recreation.....	2,717,368	-	434,220	3,151,588
Pension benefits.....	20,836,787	-	-	20,836,787
Employee benefits.....	24,159,735	-	-	24,159,735
State and county charges.....	7,987,790	-	-	7,987,790
Debt service:				
Principal.....	4,600,181	280,000	-	4,880,181
Interest.....	2,708,247	125,504	-	2,833,751
<b>TOTAL EXPENDITURES.....</b>	<b>160,403,125</b>	<b>5,471,595</b>	<b>25,424,979</b>	<b>191,299,699</b>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES.....</b>	<b>1,343,568</b>	<b>307,373</b>	<b>(4,008,776)</b>	<b>(2,357,835)</b>
<b>OTHER FINANCING SOURCES (USES):</b>				
Proceeds from bonds and notes.....	-	-	10,073,053	10,073,053
Sale of capital assets.....	150,484	-	-	150,484
Transfers in.....	2,025,194	-	1,165,428	3,190,622
Transfers out.....	(748,122)	(95,356)	(1,517,927)	(2,361,405)
<b>TOTAL OTHER FINANCING SOURCES (USES).....</b>	<b>1,427,556</b>	<b>(95,356)</b>	<b>9,720,554</b>	<b>11,052,754</b>
<b>NET CHANGE IN FUND BALANCES.....</b>	<b>2,771,124</b>	<b>212,017</b>	<b>5,711,778</b>	<b>8,694,919</b>
<b>FUND BALANCES AT BEGINNING OF YEAR (as restated).....</b>	<b>23,100,171</b>	<b>8,463,340</b>	<b>5,461,306</b>	<b>37,024,817</b>
<b>FUND BALANCES AT END OF YEAR.....</b>	<b>\$ 25,871,295</b>	<b>\$ 8,675,357</b>	<b>\$ 11,173,084</b>	<b>\$ 45,719,736</b>

See notes to basic financial statements.

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS  
TO THE STATEMENT OF ACTIVITIES**

FISCAL YEAR ENDED JUNE 30, 2006

Net change in fund balances - total governmental funds.....		\$ 8,694,919
<p>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.</p>		
Capital outlay.....	9,334,147	
Depreciation expense.....	<u>(4,925,154)</u>	
Net effect of reporting capital assets.....		4,408,993
Loss on disposal of capital assets.....		(2,148,301)
<p>Revenues in the Statement of Activities that do not provide current financial resources are fully deferred in the Statement of Revenues, Expenditures and Changes in Fund Balances. Therefore, the recognition of revenue for various types of accounts receivable (i.e., real estate and personal property, motor vehicle excise, etc.) differ between the two statements. This amount represents the net change in deferred revenue.....</p>		
		1,550,340
<p>The issuance of long-term debt (e.g., bonds and leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities.</p>		
Proceeds from bonds and notes.....	(10,073,053)	
Debt service principal payments.....	4,880,181	
Amortization of deferred charge on refunding.....	<u>(116,682)</u>	
Net effect of reporting long-term debt.....		(5,309,554)
<p>Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds.</p>		
Net change in compensated absences accrual.....	(292,000)	
Net change in accrued interest on long-term debt.....	65,289	
Net change in workers' compensation accrual.....	<u>437,000</u>	
Net effect of recording long-term liabilities and amortizing deferred losses.....		<u>210,289</u>
Change in net assets of governmental activities.....		<u>\$ 7,406,686</u>

See notes to basic financial statements.

**PROPRIETARY FUNDS**  
STATEMENT OF NET ASSETS

JUNE 30, 2006

	Business-Type Activities - Enterprise Funds		
	Water	Sewer	Total
<b>ASSETS</b>			
CURRENT:			
Cash and short-term investments.....	\$ 283,847	\$ 542,783	\$ 826,630
Receivables, net of allowance for uncollectibles:			
User fees.....	6,030,124	3,327,681	9,357,805
Tax liens.....	47,318	23,411	70,729
Other assets.....	1,149	-	1,149
<b>TOTAL ASSETS.....</b>	<b>\$ 6,362,438</b>	<b>\$ 3,893,875</b>	<b>\$ 10,256,313</b>
<b>LIABILITIES</b>			
CURRENT:			
Accrued payroll.....	\$ 13,791	\$ 4,874	\$ 18,665
<b>NET ASSETS</b>			
Unrestricted.....	6,348,647	3,889,001	10,237,648
<b>TOTAL NET ASSETS.....</b>	<b>\$ 6,348,647</b>	<b>\$ 3,889,001</b>	<b>\$ 10,237,648</b>

See notes to basic financial statements.

**PROPRIETARY FUNDS**  
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

FISCAL YEAR ENDED JUNE 30, 2006

	Business-Type Activities - Enterprise Funds		
	Water	Sewer	Total
<b>OPERATING REVENUES:</b>			
Charges for services .....	\$ 7,760,415	\$ 15,550,914	\$ 23,311,329
Utility liens.....	411,936	492,722	904,658
<b>TOTAL OPERATING REVENUES .....</b>	<b>8,172,351</b>	<b>16,043,636</b>	<b>24,215,987</b>
<b>OPERATING EXPENSES:</b>			
Cost of services and administration .....	6,482,825	11,388,908	17,871,733
<b>OPERATING INCOME (LOSS).....</b>	<b>1,689,526</b>	<b>4,654,728</b>	<b>6,344,254</b>
<b>NONOPERATING REVENUES (EXPENSES):</b>			
Investment income.....	24,472	177,026	201,498
Interest expense.....	(41,937)	(113,958)	(155,895)
<b>TOTAL NONOPERATING REVENUES (EXPENSES), NET.....</b>	<b>(17,465)</b>	<b>63,068</b>	<b>45,603</b>
<b>INCOME (LOSS) BEFORE TRANSFERS.....</b>	<b>1,672,061</b>	<b>4,717,796</b>	<b>6,389,857</b>
<b>TRANSFERS:</b>			
Transfers in.....	-	81,700	81,700
Transfers out.....	(681,113)	(229,804)	(910,917)
<b>TOTAL OPERATING TRANSFERS.....</b>	<b>(681,113)</b>	<b>(148,104)</b>	<b>(829,217)</b>
<b>CHANGE IN NET ASSETS.....</b>	<b>990,948</b>	<b>4,569,692</b>	<b>5,560,640</b>
<b>NET ASSETS AT BEGINNING OF YEAR (as restated)..</b>	<b>5,357,699</b>	<b>(680,691)</b>	<b>4,677,008</b>
<b>NET ASSETS AT END OF YEAR.....</b>	<b>\$ 6,348,647</b>	<b>\$ 3,889,001</b>	<b>\$ 10,237,648</b>

See notes to basic financial statements.

**PROPRIETARY FUNDS**  
STATEMENT OF CASH FLOWS

FISCAL YEAR ENDED JUNE 30, 2006

	Business-Type Activities - Enterprise Funds		
	Water	Sewer	Total
<b><u>CASH FLOWS FROM OPERATING ACTIVITIES:</u></b>			
Receipts from customers and users.....	\$ 7,757,172	\$ 12,011,853	\$ 19,769,025
Payments to vendors.....	(6,025,372)	(11,116,819)	(17,142,191)
Payments to employees.....	(749,375)	(267,215)	(1,016,590)
<b>NET CASH FROM OPERATING ACTIVITIES.....</b>	<b>982,425</b>	<b>627,819</b>	<b>1,610,244</b>
<b><u>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</u></b>			
Transfers in.....	-	81,700	81,700
Transfers out.....	(681,113)	(229,804)	(910,917)
<b>NET CASH FROM NONCAPITAL FINANCING ACTIVITIES.....</b>	<b>(681,113)</b>	<b>(148,104)</b>	<b>(829,217)</b>
<b><u>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</u></b>			
Interest expense.....	(41,937)	(113,958)	(155,895)
<b><u>CASH FLOWS FROM INVESTING ACTIVITIES:</u></b>			
Investment income.....	24,472	177,026	201,498
<b>NET CHANGE IN CASH AND SHORT-TERM INVESTMENTS.....</b>	<b>283,847</b>	<b>542,783</b>	<b>826,630</b>
<b>CASH AND SHORT-TERM INVESTMENTS AT BEGINNING OF YEAR</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>CASH AND SHORT-TERM INVESTMENTS AT END OF YEAR</b>	<b>\$ 283,847</b>	<b>\$ 542,783</b>	<b>\$ 826,630</b>
<b><u>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH FROM OPERATING ACTIVITIES:</u></b>			
Operating income (loss).....	\$ 1,689,526	\$ 4,654,728	\$ 6,344,254
Adjustments to reconcile operating income (loss) to net cash from operating activities:			
Changes in assets and liabilities:			
Tax Liens.....	(47,318)	(23,411)	(70,729)
User fees.....	(315,595)	(3,420,208)	(3,735,803)
Other assets.....	(1,149)	-	(1,149)
Warrants payable.....	(305,713)	-	(305,713)
Accrued payroll.....	13,791	4,874	18,665
Due to other funds.....	(51,117)	(588,164)	(639,281)
<b>Total adjustments.....</b>	<b>(707,101)</b>	<b>(4,026,909)</b>	<b>(4,734,010)</b>
<b>NET CASH FROM OPERATING ACTIVITIES.....</b>	<b>\$ 982,425</b>	<b>\$ 627,819</b>	<b>\$ 1,610,244</b>

See notes to basic financial statements.

**FIDUCIARY FUNDS**  
STATEMENT OF FIDUCIARY NET ASSETS

JUNE 30, 2006

	Pension Trust Fund (as of December 31, 2005)	Private Purpose Trust Funds	Agency Funds
<b>ASSETS</b>			
CURRENT:			
Cash and short-term investments.....	\$ 17,609,405	\$ 95,041	\$ 402,695
Investments.....	134,975,496	-	-
Interest and dividends.....	32,643	-	-
Receivables, net of allowance for uncollectibles:			
Intergovernmental.....	5,986,735	-	-
<b>TOTAL ASSETS.....</b>	<b>158,604,279</b>	<b>95,041</b>	<b>402,695</b>
<b>LIABILITIES</b>			
Warrants payable.....	7,773	-	-
Accrued liabilities.....	-	-	19,275
Liabilities due depositors.....	-	-	383,420
<b>TOTAL LIABILITIES.....</b>	<b>7,773</b>	<b>-</b>	<b>402,695</b>
<b>NET ASSETS</b>			
Held in trust for pension benefits and other purposes.....	\$ 158,596,507	\$ 95,041	\$ -

See notes to basic financial statements.

**FIDUCIARY FUNDS**  
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

FISCAL YEAR ENDED JUNE 30, 2006

	Pension Trust Fund (as of December 31, 2005)	Private Purpose Trust Funds
<b>ADDITIONS:</b>		
Contributions:		
Employer.....	\$ 11,410,825	\$ -
Employee.....	4,331,225	-
Private donations.....	-	4,236
Total contributions.....	15,742,050	4,236
Net investment income (loss):		
Net change in fair value of investments.....	4,823,684	-
Interest.....	5,104,986	2,639
Total investment income (loss).....	9,928,670	2,639
Less: investment expense.....	(1,444,425)	-
Net investment income (loss).....	8,484,245	2,639
Intergovernmental.....	966,178	-
Transfers from other systems.....	386,529	-
TOTAL ADDITIONS.....	25,579,002	6,875
<b>DEDUCTIONS:</b>		
Administration.....	297,670	-
Transfers to other systems.....	1,142,839	-
Retirement benefits and refunds.....	18,019,670	-
Educational scholarships.....	-	5,904
TOTAL DEDUCTIONS.....	19,460,179	5,904
CHANGE IN NET ASSETS.....	6,118,823	971
NET ASSETS AT BEGINNING OF YEAR.....	152,477,684	94,070
NET ASSETS AT END OF YEAR.....	\$ 158,596,507	\$ 95,041

See notes to basic financial statements.

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying basic financial statements of the City of Somerville, Massachusetts (the City) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The significant City accounting policies are described herein.

**A. Reporting Entity**

The City is a municipal corporation that is governed by an elected Mayor and an eleven member Board of Alderman (Board).

For financial reporting purposes, the City has included all funds, organizations, agencies, boards, commissions and institutions. The City has also considered all potential component units for which it is financially accountable as well as other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the basic financial statements to be misleading or incomplete. As required by GAAP, these basic financial statements present the City (primary government) and its component units. One entity has been included as a component unit in the reporting entity, because of the significance of its operational and/or financial relationship.

*Blended Component Units* – Blended component units are entities that are legally separate from the City, but are so related that they are, in substance, the same as the City or entities providing services entirely or almost entirely for the benefit of the City. The following component unit is blended within the primary government:

In the Fiduciary Funds:

The Somerville Contributory Retirement System (System) was established to provide retirement benefits to City employees, the City Housing Authority employees, and their beneficiaries. The System is governed by a five-member board comprised of the City Auditor (ex-officio), two members elected by the System's participants, one member appointed by the Mayor and one member appointed by the Board members. The System is presented using the accrual basis of accounting and is reported as a pension trust fund in the fiduciary fund financial statements.

**Availability of Financial Information for Component Units**

The System did not issue a separate audited financial statement. The System issues a publicly available unaudited financial report in accordance with guidelines established by the Commonwealth of Massachusetts' (Commonwealth) Public Employee Retirement Administration Commission (PERAC). That report may be obtained by contacting the System located at 50 Evergreen Avenue, Somerville, Massachusetts 02145.

**B. Government-Wide and Fund Financial Statements*****Government-Wide Financial Statements***

The government-wide financial statements (i.e., statement of net assets and the statement of changes in net assets) report information on all of the non-fiduciary activities of the primary government and its component units. *Governmental activities* are primarily supported by taxes and intergovernmental revenues.

*Fund Financial Statements*

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though fiduciary funds are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements. Non-major funds are aggregated and displayed in a single column.

*Major Fund Criteria*

Major funds must be reported if the following criteria are met:

- If the total assets, liabilities, revenues, or expenditures/expenses of an individual governmental fund are at least 10 percent of the corresponding element (assets, liabilities, etc.) for all funds of that category or type (total governmental funds), *and*
- If the total assets, liabilities, revenues, or expenditures/expenses of the individual governmental funds are at least 5 percent of the corresponding element for all governmental funds combined.

Additionally, any other governmental fund that management believes is particularly significant to the basic financial statements may be reported as a major fund.

Internal service funds and fiduciary funds are reported by fund type.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation*Government-Wide Financial Statements*

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded when the liabilities are incurred. Real estate and personal property taxes are recognized as revenues in the fiscal year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The statement of activities demonstrates the degree to which the direct expenses of a particular 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 the following:

- Charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment.
- Grants and contributions that are restricted to meeting the operational requirements of a particular function or segment.
- Grants and contributions that are restricted to meeting the capital requirements of a particular function or segment.

Taxes and other items not identifiable as program revenues are reported as general revenues.

For the most part, the effect of interfund activity has been removed from the government-wide financial statements.

*Fund Financial Statements*

**Governmental** fund financial statements are reported using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., measurable and available). Measurable means the amount of the transaction can be determined and available means collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures are recorded when the related fund liability is incurred, except for unmatured interest on general long-term debt which is recognized when due, and certain compensated absences and claims and judgments which are recognized when the obligations are expected to be liquidated with current expendable available resources.

Real estate and personal property tax revenues are considered available if they are collected within 60 days after fiscal year-end. Investment income is susceptible to accrual. Other receipts and tax revenues become measurable and available when the cash is received and are recognized as revenue at that time.

Entitlements and shared revenues are recorded at the time of receipt or earlier if the susceptible to accrual criteria is met. Expenditure driven grants recognize revenue when the qualifying expenditures are incurred and all other grant requirements are met.

The following major governmental funds are reported:

The *general fund* is the primary operating fund. It is used to account for all financial resources, except those that are required to be accounted for in another fund.

The *community development fund* is used to account for activities of the Office of Housing and Community Development.

The nonmajor governmental funds consist of other special revenue, capital projects and permanent funds that are aggregated and presented in the *nonmajor governmental funds* column on the governmental funds financial statements. The following describes the general use of these fund types:

The *special revenue fund* is used to account for the proceeds of specific revenue sources (other than permanent funds or capital projects funds) that are restricted by law or administrative action to expenditures for specified purposes.

The *capital projects fund* is used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by Trust Funds).

The *permanent fund* is used to account for financial resources that are legally restricted to the extent that only earnings, not principal, may be used for purposes that support the governmental programs.

**Proprietary** fund financial statements are reported using the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded when the liabilities are incurred.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the proprietary funds principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

The following major proprietary funds are reported:

The *water enterprise fund* is used to account for financial activity that occurs as a result of the ongoing operations within the water department.

The *sewer enterprise fund* is used to account for the financial activity that occurs as a result of the ongoing operations within the sewer department.

**Fiduciary** fund financial statements are reported using the flow of economic resources measurement focus and use the accrual basis of accounting. Fiduciary funds are used to account for assets held in a trustee capacity for others that cannot be used to support the governmental programs.

The following fiduciary fund types are reported:

The *pension trust fund* is used to account for the activities of the System, which accumulates resources to provide pension benefits to eligible retirees and their beneficiaries.

The *private-purpose trust fund* is used to account for trust arrangements that exclusively benefit individuals, private organizations, or other governments. Some of these trusts have donor restrictions and trustee policies that do not allow the endowment portion and any unrealized appreciation to be spent. The donor restrictions and trustee policies only allows the trustees to authorize spending of the realized investment earnings. The City's educational scholarship trusts are accounted for in this fund.

The *agency fund* is used to account for assets held in a purely custodial capacity.

#### *Government-Wide and Fund Financial Statements*

For the government-wide financial statements, and proprietary and fiduciary fund accounting, all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or prior to November 30, 1989, are applied, unless those pronouncements conflict with or contradict GASB pronouncements.

#### D. Cash and Investments

##### *Government-Wide and Fund Financial Statements*

Cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with an original maturity of three months or less from the date of acquisition. Investments are carried at fair value.

#### E. Accounts Receivable

##### *Government-Wide and Fund Financial Statements*

The recognition of revenue related to accounts receivable reported in the government-wide financial statements and the fiduciary funds financial statements are reported under the accrual basis of accounting. The recognition of revenue related to accounts receivable reported in the governmental funds financial statements are reported under the modified accrual basis of accounting.

**Real Estate, Personal Property Taxes and Tax Liens**

Real estate and personal property taxes are levied and based on values assessed on January 1<sup>st</sup> of every year. Assessed values are established by the Board of Assessor's for 100% of the estimated fair market value. Taxes are due on August 1<sup>st</sup>, November 1<sup>st</sup>, February 1<sup>st</sup> and May 1<sup>st</sup> and are subject to penalties and interest if they are not paid by the respective due date. Real estate and personal property taxes levied are recorded as receivables in the fiscal year of the levy.

Real estate tax liens are processed six months after the close of the valuation year on delinquent properties and are recorded as receivables in the fiscal year they are processed.

Real estate receivables are secured via the tax lien process and are considered 100% collectible. Accordingly, an allowance for uncollectibles is not reported.

Personal property taxes cannot be secured through the lien process. The allowance of uncollectibles is estimated based on historical trends and specific account analysis.

**Motor Vehicle Excise**

Motor vehicle excise taxes are assessed annually for each vehicle registered in the City and are recorded as receivables in the fiscal year of the levy. The Commonwealth is responsible for reporting the number of vehicles registered and the fair values of those vehicles. The tax calculation is the fair value of the vehicle multiplied by \$25 per \$1,000 of value. The allowance for uncollectibles is estimated based on historical trends and specific account analysis.

**Water and Sewer**

User fees are levied monthly based on individual meter readings and are subject to penalties and interest if they are not paid by the respective due date. Water and Sewer liens are processed in December of every year and included as a lien on the property owner's tax bill. Water and Sewer charges and liens are recorded as receivables in the fiscal year of the levy.

Since the receivables are secured via the lien process, these accounts are considered 100% collectible and therefore do not report an allowance for uncollectibles.

**Departmental and Other**

Departmental and other receivables consist primarily of parking fines and are recorded as receivables in the fiscal year accrued. The allowance of uncollectibles is estimated based on historical trends and specific account analysis.

**Intergovernmental**

Various federal and state grants for operating and capital purposes are applied for and received annually. For non-expenditure driven grants, receivables are recorded as soon as all eligibility requirements imposed by the provider have been met. For expenditure driven grants, receivables are recorded when the qualifying expenditures are incurred and all other grant requirements are met.

These receivables are considered 100% collectible and therefore do not report an allowance for uncollectibles.

**Loans**

The Office of Planning and Community Development administers loan programs that provide housing assistance to residents and capital needs assistance for small businesses. Upon issuance, a receivable is recorded for the principal amount of the loan.

Loan receivables are secured via the lien process and are considered 100% collectible. Accordingly, an allowance for uncollectibles is not reported.

F. Inventories

*Government-Wide and Fund Financial Statements*

Inventories are recorded as expenditures at the time of purchase. Such inventories are not material in total to the government-wide and fund financial statements, and therefore are not reported.

G. Capital Assets

*Government-Wide Fund Financial Statements*

Capital assets, which include land, construction in progress, land improvements, buildings, machinery and equipment, vehicles, and infrastructure (e.g., roads, water mains, sewer mains, and similar items), are reported in the applicable governmental activity column of the government-wide financial statements. Capital assets are recorded at historical cost, or at estimated historical cost, if actual historical cost is not available. Donated capital assets are recorded at the estimated fair market value at the date of donation. Construction period interest is capitalized on constructed capital assets except for the capital assets of the governmental activities column in the government-wide financial statements.

All purchases and construction costs in excess of \$10,000 are capitalized at the date of acquisition or construction, respectively, with expected useful lives of greater than one year.

Capital assets (excluding land) are depreciated on a straight-line basis. The estimated useful lives of capital assets are as follows:

<u>Capital Asset Type</u>	<u>Estimated Useful Life (in years)</u>
Land improvements.....	20-40
Books and improvements.....	10
Buildings and periodicals.....	20-40
Machinery and equipment.....	5-10
Vehicles.....	5-15
Infrastructure.....	10-50

The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend asset lives are not capitalized and are treated as expenses when incurred. Improvements are capitalized.

*Governmental Fund Financial Statements*

Capital asset costs are recorded as expenditures in the acquiring fund in the fiscal year of the purchase.

H. Interfund Receivables and Payables

During the course of its operations, transactions occur between and within individual funds that may result in amounts owed between funds.

*Government-Wide Financial Statements*

Transactions of a buyer/seller nature between and within governmental funds and internal service funds are eliminated from the governmental activities in the statement of net assets. Any residual balances outstanding between the governmental activities and business-type activities are reported in the statement of net assets as "internal balances".

*Fund Financial Statements*

Transactions of a buyer/seller nature between and within funds are *not* eliminated from the individual fund statements. Receivables and payables resulting from these transactions are classified as "Due from other funds" or "Due to other funds" on the balance sheet.

I. Interfund Transfers

During the course of its operations, resources are permanently reallocated between and within funds. These transactions are reported as operating transfers in and operating transfers out.

*Government-Wide Financial Statements*

Operating transfers between and within governmental funds are eliminated from the governmental activities in the statement of activities. Any residual balances outstanding between the governmental activities and business-type activities are reported in the statement of activities as "Transfers, net".

*Fund Financial Statements*

Operating transfers between and within funds are *not* eliminated from the individual fund statements and are reported as operating transfers in and operating transfers out.

J. Deferred Revenue

Deferred revenue at the governmental fund financial statement level represents billed receivables that do not meet the available criterion in accordance with the current financial resources measurement focus and the modified accrual basis of accounting. Deferred revenue is recognized as revenue in the conversion to the government-wide (full accrual) financial statements.

K. Net Assets and Fund Equity*Government-Wide Financial Statements (Net Assets)*

Net assets are reported as restricted when amounts that are not available for appropriation or are legally restricted by outside parties for a specific future use.

Net assets have been “restricted for” the following:

“Streets” represents amounts committed by the Commonwealth for the repair and/or construction of streets.

“Community Development” represents amounts committed by the federal Department of Housing and Urban Development (HUD) for various community development projects.

“Loans” represents community development outstanding loans receivable balances.

“Permanent funds – nonexpendable” represents the endowment portion of donor restricted trusts that support governmental programs.

“Permanent funds – expendable” represents the amount of realized and unrealized investment earnings of donor restricted trusts. The donor restrictions and trustee policies only allows the trustees to approve spending of the realized investment earnings that support governmental programs.

“Other specific purposes” represents restrictions placed on assets from outside parties.

#### *Fund Financial Statements (Fund Balances)*

Fund balances are reserved for amounts that are not available for appropriation or are legally restricted by outside parties for a specific future use. Designations of fund balance represent tentative management plans that are subject to change.

Fund balances have been “reserved for” the following:

“Encumbrances and continuing appropriations” represents amounts obligated under purchase orders, contracts and other commitments for expenditures that are being carried over to the ensuing fiscal year.

“Loans” represents community development outstanding loans receivable balances.

“Employee benefits” represents the amount accumulated for the specific purpose of providing health insurance coverage for the City’s employees and retirees.

“Perpetual permanent funds” represents amounts held in trust for which only investment earnings may be expended.

“Other specific purposes” represents restrictions placed on assets from outside parties.

Fund balances have been “designated for” the following:

“Subsequent year’s expenditures” represents amounts appropriated for the fiscal year 2007 operating budget.

#### L. Long-term debt

##### *Government-Wide and Proprietary Fund Financial Statements*

Long-term debt is reported as a liability in the government-wide statement of net assets. Material bond premiums and discounts are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount.

*Governmental Fund Financial Statements*

The face amount of governmental funds long-term debt is reported as other financing sources. Bond premiums and discounts, as well as issuance costs, are recognized in the current period. Bond premiums are reported as other financing sources and bond discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual bond proceeds received, are reported as general government expenditures.

M. Investment Income

Excluding the permanent funds, investment income derived from major and nonmajor governmental funds is legally assigned to the general fund unless otherwise directed by Massachusetts General Law (MGL).

N. Compensated Absences

Employees are granted vacation and sick leave in varying amounts based on collective bargaining agreements, state laws and executive policies.

*Government-Wide Financial Statements*

Vested or accumulated vacation and sick leave are reported as liabilities and expensed as incurred.

*Governmental Fund Financial Statements*

Vested or accumulated vacation and sick leave, which will be liquidated with expendable available financial resources, are reported as expenditures and fund liabilities.

O. Post Retirement Benefits*Government-Wide and Fund Financial Statements*

In addition to providing pension benefits, health insurance coverage is provided for retired employees and their survivors in accordance with MGL, Chapter 32, on a pay-as-you-go basis. The cost of providing health insurance is recognized by recording the employer's 90% share of insurance premiums in the general fund in the fiscal year paid. For the fiscal year ended June 30, 2006, this expense/expenditure totaled approximately \$9,576,000. There were 1242 participants eligible to receive benefits at June 30, 2006.

P. Use of Estimates*Government-Wide and Fund Financial Statements*

The preparation of basic financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure for contingent assets and liabilities at the date of the basic financial statements and the reported amounts of the revenues and expenditures/expenses during the fiscal year. Actual results could vary from estimates that were used.

Q. Individual Fund Deficits

At June 30, 2006, fund deficits exist within the Capital Projects Fund. These deficits will be funded future bond proceeds.

### R. Beginning Balance Restatement

Beginning net assets for the governmental activities has been restated to account for the activities of the water and sewer funds as business-type activities. In prior years the City accounted for the activities of the funds as a combined water/sewer major governmental fund. These funds are now properly presented as two separate enterprise funds. Beginning net assets of the governmental activities has also been restated to account for approximately \$4.0 million of capital assets previously omitted from prior year financial statements. The net effect of the restatements results in a decrease of approximately \$2.9 million to beginning net assets of the governmental activities.

The restatement for the water and sewer fund enterprise funds accounts for the increase of approximately \$945,000 to the aggregate beginning balance of the governmental funds.

### S. Total Column

#### *Government-Wide Financial Statements*

The total column presented on the government-wide financial statements represents consolidated financial information.

#### *Fund Financial Statements*

The total column on the fund financial statements is presented only to facilitate financial analysis. Data in this column is not the equivalent of consolidated financial information.

## **NOTE 2 - CASH AND INVESTMENTS**

A cash and investment pool is maintained that is available for use by all funds. Each fund type's portion of this pool is displayed on the combined balance sheet as "Cash and Short-term Investments". The deposits and investments of the trust funds are held separately from those of other funds.

Statutes authorize the investment in obligations of the U.S. Treasury, agencies, and instrumentalities, certificates of deposit, repurchase agreements, money market accounts, bank deposits and the State Treasurer's Investment Pool (the Pool). In addition, there are various restrictions limiting the amount and length of deposits and investments.

The Pool meets the criteria of an external investment pool. The Pool is administered by the Massachusetts Municipal Depository Trust (MMDT), which was established by the Treasurer of the Commonwealth who serves as Trustee. The fair value of the position in the Pool is the same as the value of the Pool shares.

### Custodial Credit Risk – Deposits

In the case of deposits, this is the risk that in the event of a bank failure, the City of Somerville's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. At fiscal year-end, the carrying amount of deposits totaled \$37,677,018 and the bank balance totaled \$40,381,405. Of the bank balance, \$413,838 was covered by Federal Depository Insurance and \$39,967,567 was exposed to custodial credit risk because it was uninsured and uncollateralized.

At December 31, 2005, carrying amount of deposits for the System totaled \$15,197,102 and the bank balance totaled \$17,850,234. All of the bank balance was covered by Federal Depository Insurance.

Investments

As of June 30, 2006, the City of Somerville had the following investments:

<u>Other Investments</u>	
MMDT .....	\$ <u>10,693,970</u>

As of December 31, 2005, the System had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturity</u>		<u>Rating</u>
		<u>1-5 Years</u>	<u>6-10 Years</u>	
<u>Debt Securities</u>				
Fixed Income Mutual Fund .....	\$ 31,888,155	\$ -	\$ 31,888,155	<b>A2</b>
State of Israel Bond.....	<u>250,000</u>	<u>250,000</u>	<u>-</u>	<b>unrated</b>
Total Debt Securities.....	32,138,155	\$ <u>250,000</u>	\$ <u>31,888,155</u>	
<u>Other Investments</u>				
Equity Mutual Funds (Domestic).....	\$ 12,820,795			
Equity Mutual Funds (International).....	8,665,112			
Equities.....	65,795,899			
Real Estate.....	15,555,535			
Money Market Mutual Funds.....	<u>2,412,303</u>			
Total Investments.....	\$ <u>137,387,799</u>			

Custodial Credit Risk – Investments

For an investment, this is the risk that, in the event of a failure by the counterparty, the City will not be able to recover the value of its investments or collateral security that are in the possession of an outside party. The City does not have custodial credit risk exposure because the City’s investment of \$10,693,970 is invested with MMDT. The City does not have a formal investment policy to manage custodial credit risk.

Of the System’s investments of \$12,820,795 in Domestic Equity Mutual Funds, \$8,665,112 in International Equity Mutual Funds, \$65,795,899 in Equity, and \$15,555,535 in Real Estate, the System has custodial credit risk exposure of \$102,837,341 because the related securities are uninsured, unregistered and held by the counterparty. The System has not adopted a formal investment policy to manage custodial credit risk.

Interest Rate Risk

Neither the City or the System, have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk

The City has not adopted a formal policy related to Credit Risk. The City does not have any debt securities as of June 30, 2006.

The System has not adopted a formal policy related to Credit Risk.

Concentration of Credit Risk

The City places no limit on the amount the government may invest in any one issuer.

**NOTE 3 – RECEIVABLES**

At June 30, 2006, receivables for the individual major governmental funds and non-major funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	Gross Amount	Allowance for Uncollectibles	Net Amount
<u>Receivables:</u>			
Real estate and personal property taxes.... \$	132,999	\$ (132,999)	\$ -
Tax liens and foreclosures.....	3,037,215	-	3,037,215
Motor vehicle excise taxes.....	2,848,406	(2,342,538)	505,868
Departmental and other.....	11,761,082	(9,769,911)	1,991,171
Intergovernmental.....	50,148,223	-	50,148,223
Loans.....	8,328,809	-	8,328,809
Total.....	\$ 76,256,734	\$ (12,245,448)	\$ 64,011,286

At June 30, 2006, receivables for the enterprise funds, including the applicable allowances for uncollectible accounts, are as follows:

	Gross Amount	Allowance for Uncollectibles	Net Amount
<u>Receivables:</u>			
Sewer..... \$	3,327,681	\$ -	\$ 3,327,681
Water.....	6,030,124	-	6,030,124
Sewer liens.....	23,411	-	23,411
Water liens.....	47,318	-	47,318
Total.....	\$ 9,428,534	\$ -	\$ 9,428,534

Governmental funds report *deferred revenue* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. At the end of the current fiscal year, the various components of *deferred revenue* reported in the governmental funds were as follows:

	General Fund	Community Development	Governmental Funds	Nonmajor Total
<u>Receivable type:</u>				
Tax liens and foreclosures.....	\$ 2,556,488	\$ -	\$ -	\$ 2,556,488
Motor vehicle excise.....	505,868	-	-	505,868
Departmental and other.....	1,991,171	-	-	1,991,171
Intergovernmental.....	37,422,000	8,662,523	1,772,765	47,857,288
Total.....	<u>\$ 42,475,527</u>	<u>\$ 8,662,523</u>	<u>\$ 1,772,765</u>	<u>\$ 52,910,815</u>

**NOTE 4 – CAPITAL ASSETS**

Capital asset activity for the fiscal year ended June 30, 2006, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
<b>Governmental Activities:</b>				
<u>Capital assets not being depreciated:</u>				
Land.....	\$ 14,243,411	\$ -	\$ -	\$ 14,243,411
Construction in progress.....	1,102,642	4,686,520	(114,206)	5,674,956
Total capital assets not being depreciated.....	<u>15,346,053</u>	<u>4,686,520</u>	<u>(114,206)</u>	<u>19,918,367</u>
<u>Capital assets being depreciated:</u>				
Land improvements.....	13,399,580	301,477	-	13,701,057
Books and periodicals.....	2,025,600	111,064	-	2,136,664
Buildings and improvements.....	117,026,447	66,706	(3,161,008)	113,932,145
Machinery and equipment.....	5,234,110	182,851	(152,299)	5,264,662
Vehicles.....	7,603,505	750,913	(443,358)	7,911,060
Infrastructure.....	54,165,945	3,348,822	-	57,514,767
Total capital assets being depreciated.....	<u>199,455,187</u>	<u>4,761,833</u>	<u>(3,756,665)</u>	<u>200,460,355</u>
<u>Less accumulated depreciation for:</u>				
Land improvements.....	(4,523,780)	(494,610)	-	(5,018,390)
Books and periodicals.....	(1,196,932)	(164,989)	-	(1,361,921)
Buildings and improvements.....	(35,926,732)	(2,963,281)	1,012,707	(37,877,306)
Machinery and equipment.....	(3,633,703)	(310,151)	152,299	(3,791,555)
Vehicles.....	(5,834,113)	(396,228)	443,358	(5,786,983)
Infrastructure.....	(37,762,609)	(595,895)	-	(38,358,504)
Total accumulated depreciation.....	<u>(88,877,869)</u>	<u>(4,925,154)</u>	<u>1,608,364</u>	<u>(92,194,659)</u>
Total capital assets being depreciated, net.....	<u>110,577,318</u>	<u>(163,321)</u>	<u>(2,148,301)</u>	<u>108,265,696</u>
Total governmental activities capital assets, net.....	<u>\$ 125,923,371</u>	<u>\$ 4,523,199</u>	<u>\$ (2,262,507)</u>	<u>\$ 128,184,063</u>

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

**Governmental Activities:**

General government.....	\$ 163,663
Public safety.....	448,927
Education.....	2,839,901
Public works.....	839,870
Human services.....	1,078
Culture and recreation.....	<u>631,715</u>

Total depreciation expense - governmental activities..... \$ 4,925,154

**NOTE 5 – INTERFUND TRANSFERS**

Interfund transfers for the fiscal year ended June 30, 2006, are summarized as follows:

<u>Operating Transfers Out:</u>	<u>Operating Transfers In:</u>			
	<u>General Fund</u>	<u>Nonmajor Governmental Fund</u>	<u>Sewer Enterprise Fund</u>	<u>Total</u>
General Fund.....	\$ -	\$ 748,122	\$ -	\$ 748,122
Community Development Fund.....	95,356	-	-	95,356
Nonmajor Governmental Funds.....	1,018,921	417,306	81,700	1,517,927
Water Enterprise Fund.....	681,113	-	-	681,113
Sewer Enterprise Fund.....	<u>229,804</u>	<u>-</u>	<u>-</u>	<u>229,804</u>
Total.....	<u>\$ 2,025,194</u>	<u>\$ 1,165,428</u>	<u>\$ 81,700</u>	<u>\$ 3,272,322</u>

Transfers relate to amounts voted to fund the fiscal year 2006 budget as well as the close out of certain funds maintained within the general ledger.

**NOTE 6 – LEASES**

Operating Leases

The City leases three buildings and a licensed parking area under several non-cancelable operating leases. The total cost of these leases for the fiscal year ended June 30, 2006, totaled \$916,931 and is reported as general government, education and public safety expenditures in the basic financial statements. The future minimum lease payments are as follows:

<u>Fiscal Years Ending June 30</u>	<u>Governmental Activities</u>
2007.....	\$ 564,750
2008.....	<u>39,667</u>
Total.....	<u>\$ 604,417</u>

**NOTE 7 – SHORT-TERM FINANCING**

Short-term debt may be authorized and issued to fund the following:

- Current operating costs prior to the collection of revenues through issuance of revenue or tax anticipation notes (RANS or TANS).
- Capital project costs and other approved expenditures incurred prior to obtaining permanent financing through issuance of bond anticipation notes (BANS) or grant anticipation notes (GANS).

Short-term loans are general obligations and carry maturity dates that are limited by statute. Interest expenditures and expenses for short-term borrowings are accounted for in the general fund and capital projects fund, respectively.

Details related to the short-term debt activity for the fiscal year ended June 30, 2006, is as follows:

Type	Purpose	Rate (%)	Due Date	Balance at June 30, 2005	Renewed/ Issued	Retired/ Redeemed	Balance at June 30, 2006
BAN	Lincoln Park School.....	2.75	08/20/05	\$ 1,300,000	\$ -	\$ 1,300,000	\$ -
BAN	High School Renovations.....	2.75	08/20/05	502,000	-	502,000	-
BAN	Homen's Renovation (2).....	2.75	08/20/05	260,000	-	260,000	-
BAN	School Renovations.....	2.75	08/20/05	100,000	-	100,000	-
BAN	Equipment.....	2.75	08/20/05	1,100,000	-	1,100,000	-
BAN	Powder House Renovations.....	2.75	08/20/05	700,000	-	700,000	-
BAN	Sewer Construction.....	2.75	08/20/05	2,200,000	-	2,200,000	-
BAN	Lincoln Park School.....	4.00	08/18/06	-	1,300,000	1,300,000	-
BAN	High School Renovations.....	4.00	08/18/06	-	470,000	-	470,000
BAN	Homen's Renovation (2).....	4.00	08/18/06	-	260,000	245,000	15,000
BAN	School Renovations.....	4.00	08/18/06	-	100,000	100,000	-
BAN	Equipment.....	4.00	08/18/06	-	1,100,000	900,000	200,000
BAN	Powder House Renovations.....	4.00	08/18/06	-	700,000	700,000	-
BAN	Sewer Construction.....	4.00	08/18/06	-	2,150,000	2,070,000	80,000
BAN	Lincoln Park School.....	4.00	08/18/06	-	7,000,000	1,700,000	5,300,000
BAN	School Renovations.....	4.00	08/18/06	-	150,000	150,000	-
BAN	Equipment.....	4.00	08/18/06	-	171,199	171,199	-
BAN	Ladder Truck.....	4.00	08/18/06	-	103,801	103,801	-
Total.....				\$ 6,162,000	\$ 13,505,000	\$ 13,602,000	\$ 6,065,000

On August 18, 2006, the City renewed the \$5,300,000 Lincoln Park School BAN and paid down the remaining outstanding BAN's. On December 18, 2006, the City renewed the \$5,300,000 Lincoln Park School BAN. The new BAN will mature on October 18, 2007 with an interest rate of 4%.

**NOTE 8 - LONG-TERM DEBT**

Under the provisions of Chapter 44, Section 10, Municipal Law authorizes indebtedness up to a limit of 5% of the equalized valuation. Debt issued in accordance with this section of the law is designated as being "inside the debt limit". In addition, however, debt may be authorized in excess of that limit for specific purposes. Such debt, when issued, is designated as being "outside the debt limit".

On August 15, 2006 the City issued \$11,120,000 of general obligation debt. Of this amount, \$7,440,000 related to short term debt outstanding at June 30, 2006. The financial statements have recognized bond proceeds in fiscal year 2006 in amount equal to the related outstanding short term debt. The balance of the general obligation debt issued subsequent to year end will be recognized as bond proceeds in fiscal year 2007.

Details related to the outstanding indebtedness at June 30, 2006, and the debt service requirements are as follows:

**Bonds and Notes Payable Schedule – Governmental Funds**

Project	Interest Rate (%)	Outstanding at June 30, 2005	Issued	Redeemed	Outstanding at June 30, 2006
Municipal Purpose - April 1, 1998.....	4.2% - 6.0%	\$ 13,905,000	\$ -	\$ 955,000	\$ 12,950,000
Municipal Purpose - February 15, 1997.....	4.2% - 7.0%	14,105,000	-	950,000	13,155,000
Water Projects - July 1, 1996.....	4.8% - 7.0%	110,000	-	110,000	-
Sewer Projects - July 1, 1996.....	4.8% - 7.0%	115,000	-	115,000	-
MWRA Notes.....	0%	4,022,987	2,633,053	520,180	6,135,860
Municipal Purpose - February 15, 2002.....	3.0% - 5.0%	23,650,000	-	1,170,000	22,480,000
General Obligation Bond - March 15, 2004.....	2.0% - 4.0%	10,230,000	-	780,001	9,449,999
Municipal Purpose - August 15, 2006.....	4.0% - 4.1%	-	7,440,000	-	7,440,000
<b>Total bonds and notes payable.....</b>		<b>66,137,987</b>	<b>10,073,053</b>	<b>4,600,181</b>	<b>71,610,859</b>
Section 108 Intergovernmental Loans.....	7.1% - 8.0%	2,620,000	-	280,000	2,340,000
<b>Total.....</b>		<b>\$ 68,757,987</b>	<b>\$ 10,073,053</b>	<b>\$ 4,880,181</b>	<b>\$ 73,950,859</b>

Debt service requirements for principal and interest for Governmental bonds payable in future fiscal years are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007.....	\$ 5,381,986	\$ 2,971,532	\$ 8,353,518
2008.....	6,245,302	2,921,167	9,166,469
2009.....	6,353,992	2,706,235	9,060,227
2010.....	6,208,991	2,489,739	8,698,730
2011.....	6,177,838	2,258,153	8,435,991
2012.....	5,851,035	2,016,430	7,867,465
2013.....	5,481,228	1,783,711	7,264,939
2014.....	5,476,423	1,542,997	7,019,420
2015.....	5,291,619	1,291,721	6,583,340
2016.....	4,731,810	1,046,827	5,778,637
2017.....	4,542,006	814,117	5,356,123
2018.....	3,142,006	582,757	3,724,763
2019.....	1,912,006	427,257	2,339,263
2020.....	1,872,006	333,257	2,205,263
2021.....	1,942,006	241,257	2,183,263
2022.....	1,995,605	146,257	2,141,862
2023.....	300,000	49,107	349,107
2024.....	300,000	36,807	336,807
2025.....	300,000	24,507	324,507
2026.....	225,000	13,716	238,716
2027.....	220,000	4,538	224,538
Total.....	\$ <u>73,950,859</u>	\$ <u>23,702,089</u>	\$ <u>97,652,948</u>

The Massachusetts Water Resource Authority (MWRA) operates an Infiltration/Inflow Financial Assistance Program for community owned collection systems. For each community approved for the project, financial assistance received from the MWRA consists of a non-interest bearing loan. During fiscal year 2006, \$3,195,553 was received from this program; of this \$562,500 was a grant. The loan is payable in ten equal annual installments. At June 30, 2006, the outstanding principal amount of these loans totaled \$6,135,860.

The Commonwealth has approved school construction assistance. The assistance program, which is administered by the Massachusetts School Building Authority, provides resources for future debt service of general obligation school bonds outstanding. During fiscal year 2006 approximately \$3,736,000 of such assistance was received. Approximately \$54,516,000 will be received in future fiscal years. Of this amount, approximately \$17,094,000 represents reimbursement of long-term interest costs, and approximately \$37,422,000 represents reimbursement of approved construction costs. Accordingly, a \$37,422,000 intergovernmental receivable and corresponding deferred revenue have been reported in governmental fund financial statements. The deferred revenue has been recognized as revenue in the conversion to the government-wide financial statements.

At June 30, 2006 the City carried \$2,340,000 of debt, issued in prior fiscal years, under the United States Department of Housing and Urban Development's (HUD) Section 108 Loan Guarantee Program. The purpose of the program is to enable local governments to provide financing to urban renewal projects operated by either the government or third party developers. Debt issued under this program is secured by future entitlement allocations to the City under HUD's Community Development Block Grant (CDBG) Program. Loan proceeds, recorded as

other financing sources in the Community Development Fund when received, are used for the revitalization of Boynton Yards. Payments on these loans are reported in the Community Development Fund as debt service expenditures in the fiscal year of payment. Debt outstanding at fiscal year-end is reported as intergovernmental loans payable on the Statement of Net Assets.

The City is subject to various debt limits by statute and may issue additional general obligation debt under the normal debt limit. At June 30, 2006, the City had the following authorized and unissued debt:

Purpose	Amount
Lincoln Park School Project.....	\$ 20,400,000
Powder House Building.....	5,800,000
Sewer.....	156,975
Communications & Equipment.....	255,000
Water/Sewer/Drainage.....	1,150,000
Ladder Truck.....	671,199
School Renovations.....	470,000
Homens Renovation.....	15,000
Street Signals.....	500,000
Sidewalks.....	500,000
Highways.....	350,000
Police Cars.....	103,000
<b>Total.....</b>	<b>\$ <u>30,371,174</u></b>

Changes in Long-term Liabilities

During the fiscal year ended June 30, 2006, the following changes occurred in long-term liabilities:

	Balance June 30, 2005	Additions	Reductions	Balance June 30, 2006	Current Portion
<b>Governmental Activities:</b>					
Long-Term Bonds and Notes.....	\$ 66,137,987	\$ 10,073,053	\$ (4,600,181)	\$ 71,610,859	\$ 5,101,986
Long-Term Intergovernmental Loans..	2,620,000	-	(280,000)	2,340,000	280,000
Workers' Compensation.....	1,811,000	-	(437,000)	1,374,000	137,400
Compensated Absences.....	2,387,000	530,700	(238,700)	2,679,000	267,900
<b>Total.....</b>	<b>\$ <u>72,955,987</u></b>	<b>\$ <u>10,603,753</u></b>	<b>\$ <u>(5,555,881)</u></b>	<b>\$ <u>78,003,859</u></b>	<b>\$ <u>5,787,286</u></b>

**NOTE 9 – RISK FINANCING**

The City 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 City carries commercial insurance.

The City is self-insured for its retirees' health insurance and workers' compensation activities. These activities are accounted for in the General Fund. Liabilities, including amounts Incurred But Not Reported (IBNR), are recorded when the claim is incurred.

(a) *Health Insurance*

The estimate of Incurred But Not Reported (IBNR) claims based on a three month claims paid average. At June 30, 2006, the amount of the liability for health insurance claims totaled \$1,451,000. This liability is the best estimate based on available information. Changes in the reported liability since July 1, 2004, are as follows:

	Balance at Beginning of Fiscal Year		Current Year Claims and Changes in Estimate		Claims Payments		Balance at Fiscal Year-End
Fiscal Year 2005.....	\$ 2,287,000	\$	21,431,889	\$	(22,039,889)	\$	1,679,000
Fiscal Year 2006.....	1,679,000		27,001,321		(27,229,321)		1,451,000

(b) *Workers' Compensation*

Workers' compensation claims are administered by a third party administrator and are funded on a pay-as-you-go basis from annual appropriations. The estimated future workers' compensation liability is based on history and injury type. At June 30, 2006, the amount of the liability for workers' compensation claims totaled \$1,374,000. Changes in the reported liability since July 1, 2004, are as follows:

	Balance at Beginning of Fiscal Year		Current Year Claims and Changes in Estimate		Claims Payments		Balance at Fiscal Year-End
Fiscal Year 2005.....	\$ 429,000	\$	1,869,501	\$	(487,501)	\$	1,811,000
Fiscal Year 2006.....	1,811,000		4,790		(441,790)		1,374,000

**NOTE 10 - PENSION PLAN**

*Plan Description* - The City contributes to the System, a cost-sharing multiple-employer defined benefit pension plan administered by the Somerville Contributory Retirement Board. Substantially all employees are members of the System, except for public school teachers and certain administrators who are members of the Massachusetts Teachers Retirement System, to which the City does not contribute. Pension benefits and administrative expenses paid by the Teachers Retirement Board are the legal responsibility of the Commonwealth. The amount of these on-behalf payments totaled \$9,899,080 for the fiscal year ended June 30, 2006, and, accordingly, are reported in the general fund as intergovernmental revenues and pension expenditures.

The System provides retirement, disability and death benefits to plan members and beneficiaries. Chapter 32 of the MGL assigns authority to establish and amend benefit provisions of the plan. Cost-of-living adjustments granted between 1981 and 1997 and any increase in other benefits imposed by the Commonwealth's state law during those years are borne by the Commonwealth and are deposited into the pension fund. Cost-of-living adjustments granted after 1997 must be approved by the Somerville Contributory Retirement Board and are borne by the System. The System issues a publicly available unaudited financial report in accordance with guidelines established by the Commonwealth's PERAC. That report may be obtained by contacting the System located at 50 Evergreen Avenue, Somerville, Massachusetts 02145.

At December 31, 2005, the System's membership consists of the following:

Active members.....	1129
Inactive members.....	284
Retirees and beneficiaries currently receiving benefits.....	<u>949</u>
 Total.....	 <u><u>2362</u></u>

*Funding Policy* - Plan members are required to contribute to the System at rates ranging from 5% to 11% of annual covered compensation. The City is required to pay into the System its share of the system-wide actuarial determined contribution that is apportioned among the employers based on active current payroll. Administrative expenses are funded through investment earnings. The current and two preceding fiscal years apportionment of the annual pension cost between the two employers required the City to contribute approximately 93% of the total. Chapter 32 of the MGL governs the contributions of plan members and the City.

*Annual Pension Cost* - The City's contributions to the System for the fiscal years ended June 30, 2006, 2005, and 2004 were \$10,347,418, \$9,588,751, and \$8,622,772, respectively, which equaled its required contribution for each fiscal year. At June 30, 2006, the City did not have a net pension obligation. The required contribution was determined as part of the January 1, 2004, actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included an 8.25% investment rate of return and projected salary increases of 5.00% per year. The actuarial value of the System's assets was determined using the fair value of the assets. The System's unfunded actuarial accrued liability is being amortized as a level percentage of projected payrolls. The remaining amortization period at January 1, 2006, was 19 years.

**Schedule of Funding Progress (Dollar amounts in thousands)**

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (AAL) Entry Age (B)	Unfunded AAL (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a Percentage of Covered Payroll ((B-A)/C)
01/01/04	\$ 145,900	\$ 246,900	\$ 101,000	\$ 59.1%	\$ 43,900	230.1%
01/01/01	134,400	204,500	70,100	65.7%	44,800	156.5%
01/01/98	103,300	168,700	65,400	61.2%	39,000	167.7%
01/01/97	89,400	137,700	48,300	64.9%	36,750	131.4%
01/01/96	79,500	136,900	57,400	58.1%	33,630	170.7%
01/01/95	66,400	127,200	60,800	52.2%	35,700	170.3%
01/01/94	68,000	121,700	53,700	55.9%	27,200	197.4%

Funding progress is reported based on the biennial actuarial valuation performed by the System, and is being accumulated on a biennial basis.

*Noncontributory Retirement Allowance* – The City pays the entire retirement allowance for certain retirees who are eligible for noncontributory benefits and are not members of the System. The general fund expenditure for fiscal year 2006 totaled approximately \$564,000.

**NOTE 11 - COMMITMENTS**

The City has entered into an agreement with Waste Management of Massachusetts, Inc. to direct the acceptable waste it collects to a transfer station. The City is charged a flat rate per ton that is subject to increase annually

equal to but not to exceed any average net increase in the Consumer Price Index for Urban Wage Earners. There are no minimum tonnage requirements that the City must comply with.

The School Department has entered into an agreement with TransComm, Inc. to provide for the transportation of its students. The contract bears an annual cost of approximately \$1,300,000 and expires on June 30, 2007.

The City has entered into, or is planning to enter into, contracts totaling approximately \$24,000,000 for the reconstruction of the Lincoln School, for the renovation of the Homens building, for the renovation of the Powder House building and for various street and sidewalk projects throughout the City.

## **NOTE 12 - CONTINGENCIES**

The City participates in a number of federal award programs. Although the grant programs have been audited in accordance with the provisions of the Single Audit Act Amendments of 1996 through June 30, 2006, these programs are still subject to financial and compliance audits. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although it is expected such amounts, if any, to be immaterial.

Various legal actions and claims are pending. Litigation is subject to many uncertainties, and the outcome of individual litigated matters is not always predictable. Although the amount of liability, if any, at June 30, 2006, cannot be ascertained, management believes any resulting liability should not materially affect the financial position at June 30, 2006.

## **NOTE 13 – FUTURE IMPLEMENTATION OF NEW GASB PRONOUNCEMENTS**

During fiscal year 2006, the following GASB pronouncements were implemented:

GASB Statement #42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This pronouncement did not impact the basic financial statements.

GASB Statement #44, *Economic Condition Reporting: The Statistical Section*. This new GASB establishes and modifies requirements related to supplementary information presented in a statistical section. The presentation of a statistical section was not required by this pronouncement. This pronouncement did not impact the basic financial statements.

GASB Statement # 46, *Net Assets Restricted by Legislation an amendment of GASB Statement No. 34*. This Statement clarified that a legally enforceable enabling legislation restriction is one that a party external to a government—such as citizens, public interest groups, or the judiciary—can compel a government to honor. It required governments to disclose the portion of total net assets that is restricted by enabling legislation. This pronouncement did not impact the basic financial statements.

GASB Statement # 47, *Accounting for Termination Benefits*. The Statement provided accounting and reporting guidance for state and local governments that offer benefits such as early retirement incentives or severance to employees that are involuntarily terminated. The Statement required that similar forms of termination benefits be accounted for in the same manner and is intended to enhance both the consistency of reporting for termination benefits and the comparability of financial statements. This pronouncement did not impact the basic financial statements.

GASB Statement #48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues* which is required to be implemented in FY2008. Management has elected to implement this GASB early. This pronouncement did not impact the basic financial statements.

*Other Future GASB Pronouncements:*

The GASB issued Statement #43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, which is required to be implemented in Fiscal 2007. Since there is no legally established separate trust for the postemployment benefit plan this pronouncement will not impact the basic financial statements.

The GASB issued Statement #45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, which is required to be implemented in Fiscal 2008. Management believes this pronouncement will require additional disclosure and impact the basic financial statements.

**NOTE 14 – RECLASSIFICATIONS AND ADJUSTMENTS**

The following adjustments and reclassifications have been made to the previously reported balances:

***Fund Financial Statements***

	June 30, 2005 Previously Reported Balances	Reclass to Other Funds	To Report Enterprise Funds On Accrual Basis	June 30, 2005 Restated Balances
Sewer Enterprise Fund.....	\$ -	\$ (680,691)	\$ -	\$ (680,691)
Water Enterprise Fund.....	-	(264,303)	5,622,002	5,357,699
Water & Sewer.....	<u>(944,994)</u>	<u>944,994</u>	<u>-</u>	<u>-</u>
Total.....	<u>\$ (944,994)</u>	<u>\$ -</u>	<u>\$ 5,622,002</u>	<u>\$ 4,677,008</u>

***Governmental Activities***

Beginning net assets for governmental activities was calculated as follows:

Total fund balances of general, special revenue, capital projects, expendable and nonexpendable trusts at June 30, 2005.....	\$ 143,978,746
<i>Add:</i>	
Capital assets previously not recorded.....	4,096,742
To establish the Water and Sewer Enterprise Funds.....	944,994
<i>Less:</i>	
Receivable adjustment related to the established Enterprise Funds.....	<u>(7,969,904)</u>
<b><i>Net assets at beginning of year - Governmental Activities.....</i></b>	<b><u>\$ 141,050,578</u></b>

# ***Required Supplementary Information***

**GENERAL FUND**  
**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -**  
**BUDGET AND ACTUAL**

FISCAL YEAR ENDED JUNE 30, 2006

	Budgeted Amounts			
	Amounts Carried forward From Prior Year	Current Year Initial Budget	Original Budget	Final Budget
<b>REVENUES:</b>				
Real estate and personal property taxes, net of tax refunds.....	\$ -	\$ 77,023,339	\$ 77,023,339	\$ 77,023,339
Tax liens.....	-	-	-	-
Motor vehicle and other excise taxes.....	-	4,375,000	4,375,000	4,375,000
Payments in lieu of taxes.....	-	-	-	-
Intergovernmental.....	-	53,304,957	53,304,957	53,304,957
Departmental and other.....	-	14,449,727	14,449,727	14,449,727
Investment income.....	-	800,000	800,000	800,000
<b>TOTAL REVENUES.....</b>	<b>-</b>	<b>149,953,023</b>	<b>149,953,023</b>	<b>149,953,023</b>
<b>EXPENDITURES:</b>				
Current:				
General government.....	1,124,644	10,715,795	11,640,439	9,438,328
Public safety.....	552,831	25,087,611	25,640,442	26,191,776
Education.....	319,820	45,000,000	45,319,820	45,259,065
Public works.....	577,934	18,157,851	18,735,785	19,751,920
Culture and recreation.....	2,144	2,230,202	2,232,346	2,759,526
Pension benefits.....	-	10,924,340	10,924,340	10,948,740
Employee benefits.....	-	26,683,983	26,683,983	26,682,483
State and county charges.....	-	8,590,803	8,590,803	8,590,803
Debt service:				
Principal.....	-	4,600,181	4,600,181	4,600,181
Interest.....	-	3,098,174	3,098,174	3,098,174
<b>TOTAL EXPENDITURES.....</b>	<b>2,577,373</b>	<b>155,088,940</b>	<b>157,666,313</b>	<b>157,320,996</b>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES.....</b>	<b>(2,577,373)</b>	<b>(5,135,917)</b>	<b>(7,713,290)</b>	<b>(7,367,973)</b>
<b>OTHER FINANCING SOURCES (USES):</b>				
Sale of assets.....	-	-	-	-
Transfers in.....	-	1,860,917	1,860,917	1,960,917
Transfers out.....	-	(416,122)	(416,122)	(716,122)
<b>TOTAL OTHER FINANCING SOURCES (USES).....</b>	<b>-</b>	<b>1,444,795</b>	<b>1,444,795</b>	<b>1,244,795</b>
<b>NET CHANGE IN FUND BALANCE.....</b>	<b>(2,577,373)</b>	<b>(3,691,122)</b>	<b>(6,268,495)</b>	<b>(6,123,178)</b>
<b>BUDGETARY FUND BALANCE, Beginning of year.....</b>	<b>-</b>	<b>19,069,564</b>	<b>19,069,564</b>	<b>19,069,564</b>
<b>BUDGETARY FUND BALANCE, End of year.....</b>	<b>\$ (2,577,373)</b>	<b>\$ 15,378,442</b>	<b>\$ 12,801,069</b>	<b>\$ 12,946,386</b>

See notes to required supplementary information.

Actual Budgetary Amounts	Amounts Carried Forward To Next Year	Variance Final Budget
\$ 76,777,383	\$ -	\$ (245,956)
986,111	-	986,111
5,272,658	-	897,658
354,342	-	354,342
52,834,555	-	(470,402)
14,418,864	-	(30,863)
1,057,635	-	257,635
<u>151,701,548</u>	<u>-</u>	<u>1,748,525</u>
9,126,650	311,678	-
25,563,283	267,085	361,408
44,946,374	85,076	227,615
18,398,962	736,016	616,942
2,714,482	6,424	38,620
10,937,707	-	11,033
26,581,557	1,200	99,726
7,987,790	-	603,013
4,600,181	-	-
2,830,595	-	267,579
<u>153,687,581</u>	<u>1,407,479</u>	<u>2,225,936</u>
<u>(1,986,033)</u>	<u>(1,407,479)</u>	<u>3,974,461</u>
150,484	-	150,484
2,025,194	-	64,277
(748,122)	-	(32,000)
<u>1,427,556</u>	<u>-</u>	<u>182,761</u>
(558,477)	(1,407,479)	4,157,222
<u>19,069,564</u>	<u>-</u>	<u>-</u>
<u>\$ 18,511,087</u>	<u>\$ (1,407,479)</u>	<u>\$ 4,157,222</u>

**Notes to Required Supplementary Information**A. Budgetary Information

Municipal Law requires the adoption of a balanced budget that is approved by the Mayor and the Board. The Mayor presents an annual budget to the Board, which includes estimates of revenues and other financing sources and recommendations of expenditures and other financing uses. The Board, which has full authority to amend and/or reject the budget or any line item, adopts the expenditure budget by majority vote.

Increases or transfers between and within departments subsequent to the approval of the annual budget, requires majority Board approval via a supplemental appropriation or Board order.

The majority of appropriations are non-continuing which lapse at the end of each fiscal year. Others are continuing appropriations for which the governing body has authorized that an unspent balance from a prior fiscal year be carried forward and made available for spending in the current fiscal year. These carry forwards are included as part of the subsequent fiscal year's original budget.

Generally, expenditures may not exceed the legal level of spending (salaries, expenses and capital) authorized for an appropriation account. However, the payment of debt service is statutorily required, regardless of whether such amounts are appropriated. Additionally, expenditures for disasters, natural or otherwise, and final judgments may exceed the level of spending authorized by two-thirds majority vote of the Board.

An annual budget is adopted for the general fund in conformity with the guidelines described above. The original fiscal year 2006 approved budget authorized \$158,082,000 in appropriations and other amounts to be raised. During fiscal year 2006, the Board also decreased appropriations totaling by approximately (\$45,000).

The City Auditor's office has the responsibility to ensure that budgetary control is maintained. Budgetary control is exercised through the accounting system.

B. Budgetary - GAAP Reconciliation

For budgetary financial reporting purposes, the Uniform Municipal Accounting System basis of accounting (established by the Commonwealth) is followed, which differs from the GAAP basis of accounting. A reconciliation of budgetary-basis to GAAP-basis results for the general fund for the fiscal year ended June 30, 2006, is presented below:

Excess (deficiency) of revenues and other financing sources (uses) over expenditures - budgetary basis.....	\$	(558,477)
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Perspective difference:

Unemployment insurance trust recorded in the General Fund for GAAP.....	2,119,050
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Basis of accounting differences:

Net change in recording 60-day receipts accrual.....	141,065
Net change in recording tax refunds payable.....	5,000
Net change in recording unrecorded liabilities.....	945,022
Short-term interest accrual.....	119,464
Recognition of revenue for on-behalf payments.....	(9,899,080)
Recognition of expenditures for on-behalf payments.....	<u>9,899,080</u>

Excess (deficiency) of revenues and other financing sources (uses) over expenditures - GAAP basis.....	\$	<u>2,771,124</u>
--	----	------------------