
Financial Section





Martin Starnes & Associates, CPAs, P.A.

A Professional Association of Certified Public Accountants and Management Consultants

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of the City Council
Salisbury, North Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salisbury, North Carolina, as of and for the year ended June 30, 2006, 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 Salisbury's management. Our responsibility is to express an opinion on these basic financial statements based on our audit. We did not audit the financial statements of Downtown Salisbury, Inc. which represents 100% of the assets, net assets and revenues of the discretely presented component unit. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for Downtown Salisbury, Inc., is based solely on the reports of the other auditors.

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. The financial statements of Downtown Salisbury, Inc. were not audited in accordance with *Government Auditing Standards*. 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 and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salisbury, North Carolina, as of June 30, 2006, and the respective changes in financial position and cash flows, where appropriate, thereof and the respective budgetary comparison for the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 10, 2006, on our consideration of City of Salisbury's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. 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 and the Law Enforcement Officers' Special Separation Allowance Schedule of Funding Progress and Schedule of Employer Contributions are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We and other auditors 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 thereon.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the basic financial statements of the City of Salisbury, North Carolina. The introductory information, combining and individual nonmajor fund financial statements and schedules and the statistical tables, as well as the accompanying schedule of expenditures of federal and State awards as required by U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the State Single Audit Implementation Act, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining and individual nonmajor fund financial statements and the accompanying schedule of expenditures of federal and State awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole. The introductory information and the statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Martin Starnes + Associates CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
August 10, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Salisbury, North Carolina, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City of Salisbury for the fiscal year ended June 30, 2006. We encourage readers to read the information presented here in conjunction with the transmittal letter which begins on page 4 and the City's financial statements, which begin on page 33.

FINANCIAL HIGHLIGHTS

- The assets of the City of Salisbury's governmental and business-type activities exceeded its liabilities at the close of the fiscal year by \$120,962,768 (*net assets*).
- The government's total net assets increased by \$2,123,496. This increase is attributable to several factors. The City's total assets increased by \$2,012,117 primarily due to the addition of new streets valued at \$1,690,000 through annexations and new development.
- As of the close of the current fiscal year, the City of Salisbury's governmental funds reported combined ending fund balances of \$7,890,159, an increase of \$1,762,540 in comparison with the prior year. Approximately 42 percent of this total amount, or \$3,310,681, is available in the General Fund for spending at the government's discretion (*unreserved fund balance*).
- At the end of the current fiscal year, the unreserved fund balance for the General Fund of \$3,310,681 was 11.3 percent of total general fund expenditures and transfers for the fiscal year.
- The City of Salisbury's total long-term debt decreased by \$204,811 (less than one percent) during the current fiscal year. The City did issue \$3,565,680 of new installment purchase debt primarily for the purpose of constructing a 14,000 square foot addition to the City's police station and renovating the existing building. This new debt was more than offset by the retirement of \$3,890,068 of existing debt.
- The City's bond rating from Standard and Poor's of "A+" was reaffirmed in March 2006. The City's current bond ratings by other rating agencies are "A+" from Fitch Ratings (reaffirmed in July 2005) and "A1" from Moody's Investors Service (reaffirmed in March 2003).

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Salisbury's basic financial statements. The City's basic financial statements consist of three components: 1) government-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. The basic financial statements present two different views of the City through the use of government-wide statements and fund financial statements. In addition to the basic financial statements, this report contains other supplemental information that will enhance the reader's understanding of the financial condition of the City of Salisbury.

BASIC FINANCIAL STATEMENTS

The basic financial statements include two kinds of statements that present different views of the City.

The first two statements (Exhibits A-1 and A-2) in the basic financial statements are the *Government-wide Financial Statements*. They provide both short and long-term information about the City's overall financial status, in a manner similar to a private-sector business.

The next statements (Exhibits A-3 through A-11) are *Fund Financial Statements*. These statements focus on the activities of the individual parts of the City's government. These statements provide more detail than the government-wide statements. There are three parts to the Fund Financial Statements: 1) the governmental funds statements; 2) the proprietary fund statements; and 3) the fiduciary fund statements.

The governmental funds statements tell how general government services like public safety were financed in the short term as well as what remains available for future spending. The proprietary fund statements offer short and long-term financial information about the activities the government operates like businesses, the water and sewer system and the transit system. The fiduciary fund statements provide information about the financial relationships – like the pension trust for the City's law enforcement officers – in which the City acts solely as a trustee for the benefit of others, to whom the resources in question belong.

The next section of the basic financial statements is the notes. The notes to the financial statements explain in detail some of the data contained in those statements. After the notes, supplemental information is provided to show details about the City's individual funds. Budgetary information required by the General Statutes also can be found in this part of the statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide the reader with a broad overview of the City's finances, similar in format to a financial statement of a private-sector business. The government-wide statements provide short and long-term information about the City's financial status as a whole.

The two government-wide statements report the City's net assets and how they have changed. Net assets are the difference between the City's total assets and total liabilities. Measuring net assets is one way to gauge the City's financial condition.

The government-wide statements are divided into three categories: 1) governmental activities; 2) business-type activities; and 3) a component unit. The governmental activities include most of the City's basic services such as public safety, parks and recreation, environmental protection, community and economic development, and general administration. Property taxes, sales taxes, and state and federal grant funds finance most of these activities. The business-type activities are those services that the City charges fees to customers to help cover all or most of the cost of the services provided. These include the water and sewer and mass transit services offered by the City of Salisbury. The final category is the component unit. The City's component unit, Downtown Salisbury, Inc., is important to the City because it serves the interests of merchants and property owners in the downtown area. Although legally separate from the City, Downtown

Salisbury Inc.'s revenue consists largely of a municipal service district tax levy and a supplemental appropriation from the City, both of which must be approved by City Council.

FUND FINANCIAL STATEMENTS

The fund financial statements provide a more detailed look at the City's most significant activities. 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 Salisbury, like all other governmental entities in North Carolina, uses fund accounting to ensure and reflect compliance with finance-related legal requirements, such as the General Statutes or the City's budget ordinance. All of the funds of the City of Salisbury can be divided into two categories: governmental funds and proprietary funds.

Governmental Funds – Governmental funds are used to account for those functions reported as governmental activities in the government-wide financial statements. Most of the City's basic services are accounted for in governmental funds. These funds focus on how assets can readily be converted into cash flow in and out, and what monies are left at year-end that will be available for spending in the next year. Governmental funds are reported using an accounting method called *modified accrual accounting* which provides a short-term spending focus. As a result, the governmental fund financial statements give the reader a detailed short-term view that helps him or her determine if there are more or less financial resources available to finance the City's programs. The relationship between government activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is described in a reconciliation that is a part of the fund financial statements.

The City of Salisbury adopts an annual budget for its General Fund, as required by the General Statutes. The budget is a legally adopted document that incorporates input from the various departments of the City, the management of the City, and the decisions of City Council about which services to provide and how to pay for them. It also authorizes the City to obtain funds from identified sources to finance these current period activities. The budgetary statement provided for the General Fund demonstrates how well the City complied with the budget ordinance and whether or not the City succeeded in providing the services as planned when the budget was adopted. The budgetary comparison statement uses the budgetary basis of accounting and is presented using the same format, language, and classifications as the legal budget document. The statement shows four columns: 1) the original budget as adopted by the board; 2) the final budget as amended by the board; 3) the actual resources, charges to appropriations, and ending balances in the General Fund; and 4) the difference or variance between the final budget and the actual resources and charges. To account for the difference between the budgetary basis of accounting and the modified accrual basis, a reconciliation showing the differences in the reported activities is shown at the end of the budgetary statement.

Proprietary Funds – The City of Salisbury has two different kinds of proprietary funds. *Enterprise Funds* are used to report the same functions presented as business-type activities in the government-wide financial statements. The City of Salisbury uses enterprise funds to account for its water and sewer activity and for its mass transit operations. These funds are the same as those functions shown in the business-type activities in the Statement of Net Assets and the Statement of Activities. *Internal Service Funds* are an accounting device used to accumulate and allocate costs internally among the functions of the City of Salisbury. The City uses internal service funds to account for two activities – its self-insured health insurance and worker compensation insurance. Because most of the costs of these operations are attributable to

governmental rather than business-type activities, the internal service fund has been included within the governmental activities in the government-wide financial statements.

Fiduciary Funds – The City is the trustee, or fiduciary for its Law Enforcement Officers’ Special Separation Allowance, its Boards and Commissions, the Municipal Service District, and the Town of East Spencer’s water and sewer operations. All of the City’s fiduciary activities are reported in the Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets on pages 43 and 44. We excluded these activities from the City’s other financial statements because the City cannot use these assets to finance its operations. The City is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

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. The notes to the financial statements are on pages 45-65 of this report.

Other Information – In addition to the basic financial statements and accompanying notes, this report includes certain required supplementary information concerning the City of Salisbury’s progress in funding its obligation to provide pension benefits to its employees. Required supplementary information can be found on pages 69-70 of this report.

THE CITY OF SALISBURY’S NET ASSETS

Figure 1

	Governmental Activities		Business-Type Activities		Total	
	2006	2005	2006	2005	2006	2005
Current and other assets	\$ 12,653,473	\$ 10,152,104	\$ 11,019,529	\$ 12,488,903	\$ 23,673,002	\$ 22,641,007
Capital assets	41,442,415	38,079,383	117,303,008	119,685,918	158,745,423	157,765,301
Total assets	\$ 54,095,888	\$ 48,231,487	\$128,322,537	\$132,174,821	\$182,418,425	\$180,406,308
Long-term liabilities outstanding	\$ 11,624,644	\$ 8,162,430	\$ 45,106,211	\$ 47,807,940	\$ 56,730,855	\$ 55,970,370
Other liabilities	3,093,316	2,999,174	1,631,486	2,597,492	4,724,802	5,596,666
Total liabilities	\$ 14,717,960	\$ 11,161,604	\$ 46,737,697	\$ 50,405,432	\$ 61,455,657	\$ 61,567,036
Net assets:						
Invested in capital assets, net of related debt	\$ 32,777,082	\$ 31,657,961	\$ 72,574,520	\$ 71,848,222	\$105,351,602	\$103,506,183
Unrestricted	6,600,846	5,411,922	9,010,320	9,921,167	15,611,166	15,333,089
Total net assets	\$ 39,377,928	\$ 37,069,883	\$ 81,584,840	\$ 81,769,389	\$120,962,768	\$118,839,272
Total liabilities and net assets	\$ 54,095,888	\$ 48,231,487	\$128,322,537	\$132,174,821	\$182,418,425	\$180,406,308

As noted earlier, net assets may serve over time as one useful indicator of a government’s financial condition. The assets of the City of Salisbury exceeded liabilities by \$120,962,768 as of June 30, 2006, an increase of \$2,123,496 from the fiscal year ended June 30, 2005.

The largest portion of the City’s net assets (87.1%) reflects the City’s investment in capital assets (e.g. land, buildings, machinery, equipment, water and sewer treatment facilities, and water and sewer lines), less any related debt still outstanding that was issued to acquire or build those items. The City of Salisbury uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

Although the City of Salisbury's investment in its capital assets is reported net of the outstanding related debt, the resources needed to repay that debt must be provided by other sources, since the capital assets cannot be used to liquidate these liabilities. The remaining 12.9% of the City's net assets, \$15,611,166, is unrestricted.

Several particular aspects of the City's financial operations positively influenced the total unrestricted governmental net assets:

- Continued diligence in the collection of property taxes by maintaining a tax collection percentage of 97.25%, which is comparable to the statewide average of 97.10%.
- Increased property tax revenues of \$990,669 due primarily to economic growth and annexation.
- Continued low cost of debt due to the City's excellent bond ratings.

CITY OF SALISBURY CHANGES IN NET ASSETS

Figure 2

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Revenues:						
Program revenues:						
Charges for services	\$ 5,470,741	\$ 5,182,213	\$17,869,927	\$15,406,303	\$ 23,340,668	\$ 20,588,516
Operating grants and contributions	1,943,637	2,007,717	452,326	405,706	2,395,963	2,413,423
Capital grants and contributions	2,406,145	2,150,557	43,765	5,040,339	2,449,910	7,190,896
General revenues:						
Property taxes	14,580,037	13,589,368	-	-	14,580,037	13,589,368
Other taxes	4,755,926	4,410,547	-	-	4,755,926	4,410,547
Intergovernmental revenue	2,731,869	2,848,989	-	-	2,731,869	2,848,989
Other	554,494	327,317	345,381	1,501,505	899,875	1,828,822
Total revenues	<u>\$32,442,849</u>	<u>\$30,516,708</u>	<u>\$18,711,399</u>	<u>\$22,353,853</u>	<u>\$ 51,154,248</u>	<u>\$ 52,870,561</u>
Expenses:						
General government	\$ 6,620,291	\$ 6,575,855	\$ -	\$ -	\$ 6,620,291	\$ 6,575,855
Public safety	10,559,567	10,444,970	-	-	10,559,567	10,444,970
Transportation	5,718,272	4,659,387	-	-	5,718,272	4,659,387
Environmental protection	1,785,667	1,653,027	-	-	1,785,667	1,653,027
Culture and recreation	2,637,583	2,566,970	-	-	2,637,583	2,566,970
Community and economic development	2,260,752	2,099,674	-	-	2,260,752	2,099,674
Education	42,342	42,342	-	-	42,342	42,342
Interest on long-term debt	297,212	306,022	-	-	297,212	306,022
Water and sewer	-	-	18,131,596	17,063,018	18,131,596	17,063,018
Mass transit	-	-	977,470	817,899	977,470	817,899
Total expenses	<u>\$29,921,686</u>	<u>\$28,348,247</u>	<u>\$19,109,066</u>	<u>\$17,880,917</u>	<u>\$ 49,030,752</u>	<u>\$ 46,229,164</u>
Change in net assets before transfers	\$ 2,521,163	\$ 2,168,461	\$ (397,667)	\$ 4,472,936	\$ 2,123,496	\$ 6,641,397
Transfers	(213,118)	(173,570)	213,118	173,570	-	-
Change in net assets	\$ 2,308,045	\$ 1,994,891	\$ (184,549)	\$ 4,646,506	\$ 2,123,496	\$ 6,641,397
Net assets, July 1	37,069,883	35,074,992	81,769,389	77,122,883	118,839,272	112,197,875
Net assets, June 30	<u>\$39,377,928</u>	<u>\$37,069,883</u>	<u>\$81,584,840</u>	<u>\$81,769,389</u>	<u>\$120,962,768</u>	<u>\$118,839,272</u>

Governmental activities - Governmental activities increased the City's net assets by \$2,308,045. This increase is primarily attributable to the increase in infrastructure assets due to annexation and new development contributed by developers.

Business-type activities - Business-type activities decreased the City's net assets by \$184,549 which is less than one percent of the prior year's net assets.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

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

Governmental Funds

The focus of the City of Salisbury's governmental funds is to provide information on near-term inflows, outflows, and balances of usable resources. Such information is useful in assessing the City of Salisbury's financing requirements. Specifically, unreserved fund balance can be a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the chief operating fund of the City of Salisbury. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$3,310,681, while total fund balance for the General Fund reached \$7,184,363. 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 11.3 percent of total General Fund expenditures and transfers, while total fund balance represents 24.8 percent of that same amount.

At June 30, 2006, the governmental funds of the City of Salisbury reported a combined fund balance of \$7,890,159, a \$1,762,540 or 28.8 percent increase over last year. This increase in fund balance is primarily due unspent proceeds from the new \$3,565,680 installment purchase financing in the Capital Project Fund.

General Fund Budgetary Highlights - During the fiscal year, the City revised the budget on several occasions. Generally, budget amendments fall into one of three categories: 1) amendments made to adjust the estimates that are used to prepare the original budget ordinance once exact information is available; 2) amendments made to recognize new funding amounts from external sources, such as Federal and State grants; and 3) increases in appropriations that become necessary to maintain services.

Total amendments to the General Fund increased revenues and other sources of funds and expenditures by \$1,356,674. The difference between the original budget and the final amended budget can be briefly summarized as follows:

- Fund balance in the amount of \$926,100 was appropriated for the construction of a new fire station.
- Fund balance in the amount of \$205,000 was appropriated for the purchase of property.
- Federal asset forfeiture funds, which are restricted for use for the Police Department, in the amount of \$129,410 were appropriated for the new addition to the police station and for various equipment purchases.
- Funds were appropriated for various donations totaling \$67,921.

Revenues were less than the budgeted amounts primarily because some appropriated grant funds and donations had not been earned and therefore, not received by June 30, 2006. The City had not earned these funds because the related expenditures had not been made. Therefore, these

unearned grants had no effect on the General Fund's change in fund balance, which increased by \$399,943 during the fiscal year ended June 30, 2006.

Proprietary Funds

The City of Salisbury's proprietary funds provide the same type of information found in the government-wide statements but in more detail. Unrestricted net assets of the Proprietary Funds and the Water and Sewer Fund at the end of the fiscal year amounted to \$9,010,320, a decrease of \$910,847. This decrease in unrestricted net assets is a result to the expenditures of cash balances for the construction of water and sewer infrastructure assets. The total net assets of the Mass Transit Fund decreased by \$191,990, primarily due to the depreciation of four new buses purchased in 2005. Other factors concerning the finances of these two funds have been addressed in the discussion of the City of Salisbury's business-type activities.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets - The City of Salisbury's investment in capital assets for its governmental and business-type activities as of June 30, 2006 totals \$158,745,423 (net of accumulated depreciation). These assets include buildings, roads and bridges, land, machinery and equipment, park facilities, vehicles, water and sewer treatment facilities, and water and sewer lines. The City's capital assets in the governmental-type assets increased by 8.8 percent, whereas capital assets in the business-type activities decreased by 2 percent due to depreciation.

Major capital asset transactions during the year include the following additions (there were no significant demolitions or disposals):

- Completion of several water and sewer construction projects, including extension to the Highway 70 annexation area. The completion of these projects resulted in a decrease in construction in progress of \$3,714,888 from the previous year.
- General infrastructure taken over via annexation and contributions from developers included streets valued at \$1,690,000.
- Purchase of a new fire truck for \$397,730.
- Purchase of various other vehicles and motorized equipment, totaling \$936,357, including ten police cars, a new garbage truck, and a new camera van for the Water and Sewer Department.
- Purchase of property in downtown Salisbury for \$205,000.

CITY OF SALISBURY'S CAPITAL ASSETS

(net of depreciation)

Figure 3

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Land	\$ 3,362,646	\$ 3,157,445	\$ 2,072,067	\$ 2,072,067	\$ 5,434,713	\$ 5,229,512
Construction in progress	3,232,117	415,161	820,711	4,535,599	4,052,828	4,950,760
Buildings	1,238,728	1,300,888	1,656,680	1,858,084	2,895,408	3,158,972
Improvements other than buildings	7,461,889	7,549,310			7,461,889	7,549,310
Equipment	1,647,676	2,185,117	278,107	453,860	1,925,783	2,638,977
Vehicles and motorized equipment	2,203,830	1,752,543	1,829,158	2,044,414	4,032,988	3,796,957
Infrastructure	22,295,529	21,718,919	110,646,285	108,721,894	132,941,814	130,440,813
Total	\$41,442,415	\$38,079,383	\$117,303,008	\$119,685,918	\$158,745,423	\$157,765,301

Additional information on the City's capital assets can be found in note 2.A.4. of the Basic Financial Statements.

Long-term Debt - As of June 30, 2006, the City of Salisbury had total long-term debt outstanding of \$54,588,551 (not including compensated absences). Of this, \$12,667,712 is general obligation debt backed by the full faith and credit of the City and \$19,774,236 represents bonds secured solely by specified revenue sources (i.e. revenue bonds).

CITY OF SALISBURY'S OUTSTANDING DEBT

(not including compensated absences)

Figure 4

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
General obligation bonds	\$ 2,075,000	\$ 2,265,000	\$10,592,712	\$11,934,124	\$12,667,712	\$14,199,124
Revenue bonds	-	-	19,774,236	20,383,247	19,774,236	20,383,247
State bond loans	-	-	11,537,566	12,420,072	11,537,566	12,420,072
Capital leases	-	-	2,799,885	3,070,497	2,799,885	3,070,497
Installment purchases	7,277,152	4,156,422	-	-	7,277,152	4,156,422
HUD Section 108 loan	532,000	564,000	-	-	532,000	564,000
Total	\$ 9,884,152	\$ 6,985,422	\$44,704,399	\$47,807,940	\$54,588,551	\$54,793,362

The City of Salisbury's total outstanding debt decreased by \$204,811 (less than one percent) during the past fiscal year. The City did borrow \$3,565,680 on new installment purchase financing for the purpose of constructing and improving facilities and the police station.

As mentioned in the financial highlights section of this document, the City of Salisbury maintained its A1 bond rating from Moody's Investor Service and A+ rating from Standard and Poor's Corporation and Fitch Ratings. These bond ratings are a clear indication of the sound financial condition of the City of Salisbury. This achievement is a primary factor in keeping interest costs low on the City's outstanding debt.

North Carolina general statutes limit the amount of general obligation debt that a unit of government can issue to 8 percent of the total assessed value of taxable property located within that government's boundaries. The legal debt margin for the City of Salisbury is \$165,834,979.

Additional information regarding the City of Salisbury's long-term debt can be found in Note 2.B.5 of this report.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The following key economic indicators reflect the growth and prosperity of the City.

- Average unemployment in Rowan County for the fiscal year ended June 30, 2006, was 6.6%, which is a slight increase from 6.0% a year ago. The average unemployment for the State of North Carolina for the past fiscal year was 5%.
- The occupancy rates for first floor office and retail space in the City's downtown area continues to be approximately 95%.
- Inflationary trends in the region compare favorably to national indices.

BUDGET HIGHLIGHTS FOR THE FISCAL YEAR ENDING JUNE 30, 2007

Governmental Activities

General Fund - Property taxes, benefiting from economic growth and a 1-cent tax rate increase, will lead the way to an overall 11% projected increase in General Fund revenues. Current year property taxes are projected to increase by over \$420,000, or 3%. Continued increases in local sales tax revenues are expected to add an additional \$265,000 in revenue.

Expenditures in the General Fund are expected to rise approximately 13 percent to \$32,858,129. Personnel cost in the General Fund will increase by about \$860,000 due to City Council's approval of an average three percent merit raise. Health insurance costs will increase almost ten percent in the new fiscal year. The City is currently building new facilities for the police and fire departments. Both construction projects will be completed in the next fiscal year. The new fire station is being built entirely with fund balance and the City will spend approximately \$800,000 of that surplus in FY07 to complete this project. A new pumper truck for the fire department will cost \$670,000. The City plans to spend \$500,000 for a new Citizens Resource Management System (CRM) to improve the level of customer service provided to the citizens. The City will finance the new fire truck and the CRM system with installment purchase financing.

Business – Type Activities

Water and Sewer Fund - The water and sewer rates in the City will increase by 7.45%. The City is beginning to see a leveling trend in water demand after several years of declining usage. However, wastewater flows continue to decline as commercial and industrial customers are finding ways to recycle and reuse water. The decreased wastewater treatment revenues account for 1.3% of the rate increase. Operating expenses, including increased personnel cost, will account for 3.45 percent of the rate increase. In the new fiscal year the City anticipates partnering with Rowan County to extend sewer service to the County's primary growth corridor

along Interstate 85. The City intends to finance its share of the cost of this project and the projected increase in debt service cost account for the remaining 2.7 percent increase in the water and sewer rates. The City intends to issue \$15 million in revenue bonds in the next two fiscal years to fund the Interstate 85 project and other sewer extension projects.

Mass Transit Fund – Personnel costs will increase due to the approved three percent merit raise and the increase in health insurance costs. The City’s General Fund will increase its contribution to the Mass Transit Fund by \$145,451. The increased contribution from the General Fund will help to offset rising fuel cost and the cost associated with a mandatory Paratransit contract under the Americans with Disabilities Act. In the new fiscal year, the Transit Fund will begin paying for services provided by the General Fund. The City hopes to qualify for additional grant funds from the State of North Carolina to further offset the cost of providing Mass Transit services.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the City’s finances and to show the City’s accountability for the money received. Questions concerning any of the information found in this report or requests for additional information should be directed to the Management Services Director, City of Salisbury, 132 North Main Street, Salisbury, NC 28144.

A-1
CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF NET ASSETS
June 30, 2006

	Primary Government			Component
	Governmental	Business-type	Total	Unit
	Activities	Activities		Downtown Salisbury, Inc.
ASSETS				
Cash and cash equivalents	\$ 8,057,436	\$ 7,963,468	\$ 16,020,904	\$ 74,306
Taxes receivables (net)	551,631	-	551,631	-
Accrued interest receivable on taxes	69,000	-	69,000	-
Accounts receivable (net)	441,688	2,596,553	3,038,241	-
Interest receivable	29,244	31,476	60,720	-
Due from other governments	2,027,213	129,291	2,156,504	-
Inventories	201,616	290,896	492,512	-
Prepaid items	16,255	7,845	24,100	-
Intangible asset - advance funding of pension obligation	40,571	-	40,571	-
Real estate held for investment				398,507
Restricted assets:				
Cash and cash equivalents	1,218,819	-	1,218,819	44,709
Capital assets				
Land, improvements, and construction in progress	6,594,763	2,892,778	9,487,541	-
Other capital assets, net of depreciation	34,847,652	114,410,230	149,257,882	10,583
Total assets	<u>\$ 54,095,888</u>	<u>\$ 128,322,537</u>	<u>\$ 182,418,425</u>	<u>\$ 528,105</u>
LIABILITIES				
Accounts payable and accrued expenses	\$ 2,679,820	\$ 714,263	\$ 3,394,083	\$ 16,002
Unearned revenue	383,150	-	383,150	28,740
Accrued interest payable	30,346	413,866	444,212	-
Customer deposits	-	503,357	503,357	-
Long-term liabilities:				
Due within one year	1,390,084	3,302,148	4,692,232	81,247
Due in more than one year	10,234,560	41,804,063	52,038,623	203,679
Total liabilities	<u>\$ 14,717,960</u>	<u>\$ 46,737,697</u>	<u>\$ 61,455,657</u>	<u>\$ 329,668</u>
NET ASSETS				
Invested in capital assets, net of related debt	\$ 32,777,082	\$ 72,574,520	\$ 105,351,602	\$ 10,583
Restricted for:				
Capital projects	-	-	-	44,709
Unrestricted	6,600,846	9,010,320	15,611,166	143,145
Total net assets	<u>\$ 39,377,928</u>	<u>\$ 81,584,840</u>	<u>\$ 120,962,768</u>	<u>\$ 198,437</u>

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

CITY OF SALISBURY, NORTH CAROLINA

STATEMENT OF ACTIVITIES

For the Year Ended June 30, 2006

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government:				
Governmental Activities:				
General government	\$ 6,620,291	\$ 3,207,322	\$ 19,392	\$ -
Public safety	10,559,567	473,190	113,650	134,139
Transportation	5,718,272	139,704	1,068,123	2,272,006
Environmental protection	1,785,667	981,344	130,439	-
Culture and recreation	2,637,583	164,896	134,893	-
Community and economic development	2,260,752	504,285	477,140	-
Education	42,342	-	-	-
Interest on long-term debt	297,212	-	-	-
Total governmental activities	<u>\$ 29,921,686</u>	<u>\$ 5,470,741</u>	<u>\$ 1,943,637</u>	<u>\$ 2,406,145</u>
Business-type activities:				
Water and sewer	\$ 18,131,596	\$ 17,789,555	\$ -	\$ 6,663
Transit	977,470	80,372	452,326	37,102
Total business-type activities	<u>\$ 19,109,066</u>	<u>\$ 17,869,927</u>	<u>\$ 452,326</u>	<u>\$ 43,765</u>
Total primary government	<u>\$ 49,030,752</u>	<u>\$ 23,340,668</u>	<u>\$ 2,395,963</u>	<u>\$ 2,449,910</u>
Component units:				
Downtown Salisbury, Inc.	<u>\$ 384,868</u>	<u>\$ 55,840</u>	<u>\$ 90,000</u>	<u>\$ 177,577</u>
General revenues:				
Taxes:				
Property taxes, levied for general purpose				
Sales and other taxes				
Unrestricted intergovernmental revenues				
Unrestricted investment earnings				
Miscellaneous				
Transfers				
Total general revenues, special items, and transfers				
Change in net assets				
Net assets-beginning				
Net assets-ending				

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

Net (Expense) Revenue and Changes in Net Assets

Primary Government		Component Unit	
Governmental Activities	Business-type Activities	Total	Downtown Salisbury, Inc.
\$ (3,393,577)	\$ -	\$ (3,393,577)	\$ -
(9,838,588)	-	(9,838,588)	-
(2,238,439)	-	(2,238,439)	-
(673,884)	-	(673,884)	-
(2,337,794)	-	(2,337,794)	-
(1,279,327)	-	(1,279,327)	-
(42,342)	-	(42,342)	-
(297,212)	-	(297,212)	-
<u>\$ (20,101,163)</u>	<u>\$ -</u>	<u>\$ (20,101,163)</u>	<u>\$ -</u>
\$ -	\$ (335,378)	\$ (335,378)	\$ -
-	(407,670)	(407,670)	-
<u>\$ -</u>	<u>\$ (743,048)</u>	<u>\$ (743,048)</u>	<u>\$ -</u>
<u>\$ (20,101,163)</u>	<u>\$ (743,048)</u>	<u>\$ (20,844,211)</u>	<u>\$ -</u>
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (61,451)</u>
\$ 14,580,037	\$ -	\$ 14,580,037	\$ 110,041
4,755,926	-	4,755,926	-
2,731,869	-	2,731,869	-
379,137	342,961	722,098	2,778
175,357	2,420	177,777	14,522
(213,118)	213,118	-	-
<u>\$ 22,409,208</u>	<u>\$ 558,499</u>	<u>\$ 22,967,707</u>	<u>\$ 127,341</u>
\$ 2,308,045	\$ (184,549)	\$ 2,123,496	\$ 65,890
37,069,883	81,769,389	118,839,272	132,547
<u>\$ 39,377,928</u>	<u>\$ 81,584,840</u>	<u>\$ 120,962,768</u>	<u>\$ 198,437</u>

CITY OF SALISBURY, NORTH CAROLINA
BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2006

<u>ASSETS</u>	<u>Major Funds</u>			<u>Total Government Funds</u>
	<u>General Fund</u>	<u>Capital Projects Fund</u>	<u>Non-Major Fund</u>	
Cash and cash equivalents	\$ 6,629,655	\$ 1,386,966	\$ 158,473	\$ 8,175,094
Taxes receivable, net	551,631	-	-	551,631
Accounts receivable	438,885	-	2,803	441,688
Interest receivable	24,062	-	-	24,062
Due from other governments	1,988,431	-	38,782	2,027,213
Due from other fund	221,302	-	-	221,302
Inventories	201,616	-	-	201,616
Prepaid items	16,255	-	-	16,255
Total assets	<u>\$ 10,071,837</u>	<u>\$ 1,386,966</u>	<u>\$ 200,058</u>	<u>\$ 11,658,861</u>
<u>LIABILITIES AND FUND BALANCES</u>				
Liabilities:				
Accounts payable and accrued liabilities	\$ 1,952,693	\$ 642,314	\$ 17,612	\$ 2,612,619
Due to other funds	-	221,302	-	221,302
Deferred revenue	934,781	-	-	934,781
Total liabilities	<u>\$ 2,887,474</u>	<u>\$ 863,616</u>	<u>\$ 17,612</u>	<u>\$ 3,768,702</u>
Fund balances:				
Reserved for:				
Encumbrances	\$ 983,131	\$ 523,350	\$ -	\$ 1,506,481
Inventories	201,616	-	-	201,616
Prepaid items	16,255	-	-	16,255
State statute	2,672,680	-	-	2,672,680
Unreserved, General Fund	3,310,681	-	-	3,310,681
Unreserved, reported in:				
Special Revenue Fund	-	-	182,446	182,446
Total fund balances (deficit)	<u>\$ 7,184,363</u>	<u>\$ 523,350</u>	<u>\$ 182,446</u>	<u>\$ 7,890,159</u>
Total liabilities and fund balances	<u>\$ 10,071,837</u>	<u>\$ 1,386,966</u>	<u>\$ 200,058</u>	
Amounts reported for governmental activities in the statement of net assets are different because:				
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.				41,442,415
Other long-term assets are not available to pay for current-period expenditures and therefore are deferred in the funds.				
Accrued interest receivable from taxes				69,000
Intangible asset - advance funding of pension obligation				40,571
Internal service funds are used by management to charge the costs of certain activities, such as self insurance for health care and workers compensation, to individual funds. The assets and liabilities of these internal service funds are included in governmental activities in the statement of net assets.				604,019
Liabilities for earned but deferred revenues in fund statements.				551,631
Some liabilities, including bonds payable and accrued interest, are not due and payable in the current period and therefore are not reported in the funds.				
Long-term debt				(9,884,152)
Accrued interest on long-term debt				(30,346)
Long-term portion of accrued compensated absences				(1,305,369)
Net assets of governmental activities				<u>\$ 39,377,928</u>

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

CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the Year Ended June 30, 2006

	<u>Major Funds</u>		<u>Non-Major Fund</u>	<u>Total Governmental Funds</u>
	<u>General Fund</u>	<u>Capital Projects Fund</u>		
REVENUES				
Taxes	\$ 19,279,885	\$ -	\$ -	\$ 19,279,885
Intergovernmental	4,628,089	-	467,036	5,095,125
Charges for services	4,893,454	-	-	4,893,454
Miscellaneous	785,860	17,143	470,361	1,273,364
Total revenues	<u>\$ 29,587,288</u>	<u>\$ 17,143</u>	<u>\$ 937,397</u>	<u>\$ 30,541,828</u>
EXPENDITURES				
Current:				
General government	\$ 6,097,065	\$ 8,066	\$ 93,117	\$ 6,198,248
Public safety	11,394,780	2,905,921	-	14,300,701
Transportation	4,613,922	-	-	4,613,922
Environmental protection	1,801,115	-	-	1,801,115
Culture and recreation	2,601,386	-	-	2,601,386
Community and economic development	1,525,535	-	701,945	2,227,480
Education	42,342	-	-	42,342
Debt service:				
Principal	634,950	-	32,000	666,950
Interest	263,132	-	24,833	287,965
Total expenditures	<u>\$ 28,974,227</u>	<u>\$ 2,913,987</u>	<u>\$ 851,895</u>	<u>\$ 32,740,109</u>
Surplus (deficiency) of revenues over expenditures	<u>\$ 613,061</u>	<u>\$ (2,896,844)</u>	<u>\$ 85,502</u>	<u>\$ (2,198,281)</u>
OTHER FINANCING SOURCES (USES)				
Transfers to other funds	\$ (213,118)	\$ -	\$ -	\$ (213,118)
Long-term debt issued	-	3,565,680	-	3,565,680
Contributions from other fund	-	608,259	-	608,259
Total other financing sources	<u>\$ (213,118)</u>	<u>\$ 4,173,939</u>	<u>\$ -</u>	<u>\$ 3,960,821</u>
Net change in fund balance	\$ 399,943	\$ 1,277,095	\$ 85,502	\$ 1,762,540
Fund balances (deficit)-beginning	6,784,420	(753,745)	96,944	6,127,619
Fund balances-ending	<u>\$ 7,184,363</u>	<u>\$ 523,350</u>	<u>\$ 182,446</u>	<u>\$ 7,890,159</u>

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

CITY OF SALISBURY, NORTH CAROLINA
RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES

For the Year Ended June 30, 2006

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

Net changes in fund balances - total governmental funds	\$ 1,762,540
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds:	
Changes in deferred revenue for property tax revenues	50,078
Changes in accrued interest receivable on taxes	6,000
Changes in advance funding of pension obligation	7,791
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.	4,441,962
Infrastructure contributed by developers is considered a capital contribution for the statements of activities.	1,690,000
Depreciation is recognized as an expense in the statement of activities.	(2,763,134)
Internal service funds are used by management to charge costs of certain activities, such as self-insurance for health care and workers compensation, to individual funds. The net revenue of certain internal service funds is reported with governmental activities.	154,942
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction has any effect on net assets.	
Issuance of long-term debt	(3,565,680)
Repayment of principal on long-term debt	666,950
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 governmental funds.	
Change in long-term portion of compensated absences	(128,361)
Change in accrued interest payable	(9,247)
Loss on disposal of assets	(5,796)
Total changes in net assets of governmental activities	<u>\$ 2,308,045</u>

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

**CITY OF SALISBURY, NORTH CAROLINA
GENERAL FUND**

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL

For the Year Ended June 30, 2006

	General Fund			Variance with
	Original Budget	Final Budget	Actual	Final Budget Positive (Negative)
Revenues:				
Taxes	\$ 18,823,382	\$ 18,823,382	\$ 19,279,885	\$ 456,503
Intergovernmental	5,847,232	5,847,232	4,628,089	(1,219,143)
Charges for services	4,957,741	4,957,741	4,893,454	(64,287)
Miscellaneous	520,905	746,479	785,860	39,381
Total revenues	<u>\$ 30,149,260</u>	<u>\$ 30,374,834</u>	<u>\$ 29,587,288</u>	<u>\$ (787,546)</u>
Expenditures:				
Current:				
General government	\$ 6,084,004	\$ 6,302,725	\$ 6,097,065	\$ 205,660
Public safety	11,463,312	12,550,750	11,394,780	1,155,970
Transportation	5,933,923	5,933,923	4,613,922	1,320,001
Environmental protection	1,817,608	1,817,608	1,801,115	16,493
Cultural and recreation	2,575,389	2,613,104	2,601,386	11,718
Community and economic development	1,537,707	1,550,507	1,525,535	24,972
Education	42,342	42,342	42,342	-
Debt service:				
Principal retirement	642,099	642,099	634,950	7,149
Interest and other charges	266,341	266,341	263,132	3,209
Total expenditures	<u>\$ 30,362,725</u>	<u>\$ 31,719,399</u>	<u>\$ 28,974,227</u>	<u>\$ 2,745,172</u>
Surplus (deficiency) of revenues over expenditures	<u>\$ (213,465)</u>	<u>\$ (1,344,565)</u>	<u>\$ 613,061</u>	<u>\$ 1,957,626</u>
Other financing sources (uses):				
Transfers to other funds	\$ (213,118)	\$ (213,118)	\$ (213,118)	\$ -
Fund balance appropriated	426,583	1,557,683	-	(1,557,683)
Total other financing sources (uses)	<u>\$ 213,465</u>	<u>\$ 1,344,565</u>	<u>\$ (213,118)</u>	<u>\$ (1,557,683)</u>
Revenues and other sources over expenditures and other uses	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 399,943</u>	<u>\$ 399,943</u>
Fund balances, beginning of year			6,784,420	
Fund balances, end of year			<u>\$ 7,184,363</u>	

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

A-7
CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
June 30, 2006

	Enterprise Funds			Governmental Activities
	Water and Sewer Fund	Transit Fund	Total	Internal Service Funds
<u>ASSETS</u>				
Current assets:				
Cash and cash equivalents	\$ 7,956,946	\$ 6,522	\$ 7,963,468	\$ 1,101,161
Accounts receivable (net)	2,594,985	1,568	2,596,553	-
Interest receivable	31,464	12	31,476	5,182
Due from other governments	84,404	44,887	129,291	-
Prepaid items	7,845	-	7,845	-
Inventories	290,896	-	290,896	-
Total current assets	<u>\$ 10,966,540</u>	<u>\$ 52,989</u>	<u>\$ 11,019,529</u>	<u>\$ 1,106,343</u>
Noncurrent assets:				
Capital assets:				
Land	\$ 2,072,067	\$ -	\$ 2,072,067	\$ -
Buildings and improvements	155,476,641	-	155,476,641	-
Equipment	6,813,131	2,289,515	9,102,646	-
Construction in progress	820,711	-	820,711	-
Accumulated depreciation	<u>(48,690,400)</u>	<u>(1,478,657)</u>	<u>(50,169,057)</u>	<u>-</u>
Total noncurrent assets	<u>\$ 116,492,150</u>	<u>\$ 810,858</u>	<u>\$ 117,303,008</u>	<u>\$ -</u>
Total assets	<u><u>\$ 127,458,690</u></u>	<u><u>\$ 863,847</u></u>	<u><u>\$ 128,322,537</u></u>	<u><u>\$ 1,106,343</u></u>
<u>LIABILITIES</u>				
Current liabilities:				
Accounts payable and accrued liabilities	\$ 681,388	\$ 32,875	\$ 714,263	\$ 502,324
Interest payable	413,866	-	413,866	-
Bonds, notes, and loans payable	3,201,696	-	3,201,696	-
Compensated absences	89,402	11,050	100,452	-
Customer deposits	<u>503,357</u>	<u>-</u>	<u>503,357</u>	<u>-</u>
Total current liabilities	<u>\$ 4,889,709</u>	<u>\$ 43,925</u>	<u>\$ 4,933,634</u>	<u>\$ 502,324</u>
Noncurrent liabilities:				
Bonds, notes, and loans payable	\$ 41,502,703	\$ -	\$ 41,502,703	\$ -
Compensated absences	<u>268,207</u>	<u>33,153</u>	<u>301,360</u>	<u>-</u>
Total noncurrent liabilities	<u>\$ 41,770,910</u>	<u>\$ 33,153</u>	<u>\$ 41,804,063</u>	<u>\$ -</u>
Total liabilities	<u><u>\$ 46,660,619</u></u>	<u><u>\$ 77,078</u></u>	<u><u>\$ 46,737,697</u></u>	<u><u>\$ 502,324</u></u>
<u>NET ASSETS</u>				
Invested in capital assets, net of related debt	\$ 71,787,751	\$ 786,769	\$ 72,574,520	\$ -
Unrestricted	<u>9,010,320</u>	<u>-</u>	<u>9,010,320</u>	<u>604,019</u>
Total net assets	<u><u>\$ 80,798,071</u></u>	<u><u>\$ 786,769</u></u>	<u><u>\$ 81,584,840</u></u>	<u><u>\$ 604,019</u></u>

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

CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS

For the Year Ended June 30, 2006

	Enterprise Funds			Governmental Activities
	Water and Sewer Fund	Transit Fund	Total	Internal Service Funds
OPERATING REVENUES				
Charges for services	\$ 16,289,386	\$ 80,372	\$ 16,369,758	\$ 3,730,884
Water and sewer taps	602,276	-	602,276	-
Other operating revenues	897,893	2,420	900,313	-
Total operating revenues	<u>\$ 17,789,555</u>	<u>\$ 82,792</u>	<u>\$ 17,872,347</u>	<u>\$ 3,730,884</u>
OPERATING EXPENSES				
Management and administration	\$ 4,149,220	\$ 147,248	\$ 4,296,468	\$ 3,623,958
Water resources	1,571,147	-	1,571,147	-
Maintenance and construction	3,465,628	-	3,465,628	-
Wastewater collection and treatment	2,073,183	-	2,073,183	-
Environmental services	584,175	-	584,175	-
Depreciation	4,297,445	232,023	4,529,468	-
Mass transit operations	-	598,199	598,199	-
Total operating expenses	<u>\$ 16,140,798</u>	<u>\$ 977,470</u>	<u>\$ 17,118,268</u>	<u>\$ 3,623,958</u>
Operating income (loss)	<u>\$ 1,648,757</u>	<u>\$ (894,678)</u>	<u>\$ 754,079</u>	<u>\$ 106,926</u>
NONOPERATING REVENUES (EXPENSES)				
Investment earnings	\$ 342,819	\$ 142	\$ 342,961	\$ 48,016
Interest expense	(1,871,221)	-	(1,871,221)	-
Bond issuance costs	(119,577)	-	(119,577)	-
Intergovernmental revenues	-	489,428	489,428	-
Total nonoperating revenue (expenses)	<u>\$ (1,647,979)</u>	<u>\$ 489,570</u>	<u>\$ (1,158,409)</u>	<u>\$ 48,016</u>
Income (loss) before contributions and transfers	\$ 778	\$ (405,108)	\$ (404,330)	\$ 154,942
Capital contributions	6,663	-	6,663	-
Transfers from other funds	-	213,118	213,118	-
Change in net assets	\$ 7,441	\$ (191,990)	\$ (184,549)	\$ 154,942
Total net assets - beginning	<u>80,790,630</u>	<u>978,759</u>	<u>81,769,389</u>	<u>449,077</u>
Total net assets - ending	<u>\$ 80,798,071</u>	<u>\$ 786,769</u>	<u>\$ 81,584,840</u>	<u>\$ 604,019</u>

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

A-9
CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
For the Year Ended June 30, 2006

	Business-Type Activities			Governmental
	Enterprise Funds			Activities
	Water and			Internal
	Sewer Fund	Transit Fund	Total	Service Funds
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers	\$ 16,635,011	\$ 78,833	\$ 16,713,844	\$ -
Cash received from interfund services provided	-		-	3,730,884
Cash paid for goods and services	(7,500,963)	(222,396)	(7,723,359)	(3,642,714)
Cash paid to or on behalf of employees for services	(4,455,397)	(499,464)	(4,954,861)	-
Customer deposits received	252,550	-	252,550	-
Customer deposits returned	(198,768)	-	(198,768)	-
Other receipts	897,893	2,420	900,313	-
Net cash provided (used) by operating activities	<u>\$ 5,630,326</u>	<u>\$ (640,607)</u>	<u>\$ 4,989,719</u>	<u>\$ 88,170</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Transfers from other funds	\$ -	\$ 213,118	\$ 213,118	\$ -
Intergovernmental revenues	-	467,850	467,850	-
Total cash flows provided by noncapital financing activities	<u>\$ -</u>	<u>\$ 680,968</u>	<u>\$ 680,968</u>	<u>\$ -</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Acquisition and construction of capital assets	\$ (2,567,909)	\$ (34,366)	\$ (2,602,275)	\$ -
Principal paid on bond maturities and equipment contracts	(3,223,118)	-	(3,223,118)	-
Interest paid on bond maturities and equipment contracts	(1,893,019)	-	(1,893,019)	-
Developers' contributions	6,663	-	6,663	-
Net cash used by capital and related financing activities	<u>\$ (7,677,383)</u>	<u>\$ (34,366)</u>	<u>\$ (7,711,749)</u>	<u>\$ -</u>
CASH FLOWS PROVIDED BY INVESTING ACTIVITIES				
Investment earnings	<u>\$ 404,961</u>	<u>\$ 130</u>	<u>\$ 405,091</u>	<u>\$ 50,095</u>
Net increase (decrease) in cash and cash equivalents	\$ (1,642,096)	\$ 6,125	\$ (1,635,971)	\$ 138,265
Balances-beginning of the year	9,599,042	397	9,599,439	962,896
Balances-end of the year	<u>\$ 7,956,946</u>	<u>\$ 6,522</u>	<u>\$ 7,963,468</u>	<u>\$ 1,101,161</u>
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:				
Operating income (loss)	<u>\$ 1,648,757</u>	<u>\$ (894,678)</u>	<u>\$ 754,079</u>	<u>\$ 106,926</u>
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:				
Depreciation	\$ 4,297,445	\$ 232,023	\$ 4,529,468	\$ -
Changes in current assets and liabilities:				
(Increase) decrease in accounts receivable	(256,651)	(1,539)	(258,190)	-
(Increase) decrease in inventory	(41,062)	-	(41,062)	-
(Increase) decrease in due from other governments	42,118	(621)	41,497	-
Increase (decrease) in accounts payable and accrued liabilities	(144,364)	16,536	(127,828)	(18,756)
Increase (decrease) in compensated absences payable	30,301	7,672	37,973	-
Increase in customer deposits	53,782	-	53,782	-
Total adjustments	<u>\$ 3,981,569</u>	<u>\$ 254,071</u>	<u>\$ 4,235,640</u>	<u>\$ (18,756)</u>
Net cash provided (used) by operating activities	<u>\$ 5,630,326</u>	<u>\$ (640,607)</u>	<u>\$ 4,989,719</u>	<u>\$ 88,170</u>

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

CITY OF SALISBURY, NORTH CAROLINA
COMBINING STATEMENT OF NET ASSETS
FIDUCIARY FUNDS
June 30, 2006

	Fiduciary Funds	
	Pension Trust	
	Fund	Agency Funds
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 796,792	\$ 78,858
Accounts receivable	-	95,975
Interest receivable	3,173	-
 Total assets	 \$ 799,965	 \$ 174,833
 <u>LIABILITIES</u>		
Current liabilities:		
Accounts payable	\$ -	\$ 174,833
 Total liabilities	 \$ -	 \$ 174,833
 <u>NET ASSETS</u>		
Held in trust for participants	\$ 799,965	\$ -

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

CITY OF SALISBURY, NORTH CAROLINA
STATEMENT OF CHANGES IN NET ASSETS
PENSION TRUST FUND
For the Year Ended June 30, 2006

Additions:	
Employer contributions	\$ 108,259
Investment earnings	<u>28,653</u>
 Total additions	 <u>\$ 136,912</u>
 Deductions:	
Retirement payments	<u>\$ 30,051</u>
 Total deductions	 <u>\$ 30,051</u>
 Net increase	 \$ 106,861
Net assets, beginning of year	<u>693,104</u>
Net assets, end of year	<u><u>\$ 799,965</u></u>

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

CITY OF SALISBURY, NORTH CAROLINA

NOTES TO FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

The accounting policies of the City of Salisbury (City) and its discretely presented component unit conform to accounting principles generally accepted in the United States of America as applicable to governments. The following is a summary of the more significant accounting policies.

A. Reporting Entity

The City is a municipal corporation that is governed by an elected board of five city council members. As required by accounting principles generally accepted in the United States of America, these financial statements present the City and its component unit, a legally separate entity for which the City is financially accountable. The discretely presented component unit presented below is reported in a separate column in the City's financial statements in order to emphasize that it is legally separate from the City.

Discretely Presented Component Unit

Downtown Salisbury, Inc. was created to serve the interests of merchants and property owners in the downtown Salisbury area. Eight board members, one of whom is appointed by the City Council, govern the Corporation. The Corporation's revenue sources are almost entirely dependent on the City Council's approval of a municipal service district tax levy and a supplemental appropriation as part of the annual budget process. Complete financial statements for the component unit may be obtained from the unit's administrative offices at Downtown Salisbury, Inc., 100 West Innes Street Suite 300, Salisbury, NC 28144.

Related Organization

The Housing Authority of Salisbury's governing board is appointed entirely by the City's Mayor. However, the City has no further accountability for the Housing Authority's operations.

B. Basis of Presentation

Government-wide Statements – The statement of net assets and the statement of activities display information about the primary government and its component unit. These statements include the financial activities of the overall government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. These statements distinguish between the *governmental* and *business-type activities* of the City. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

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

Fund Financial Statements – The fund financial statements provide information about the City's funds, including its fiduciary funds. Separate statements for each fund category – *governmental, proprietary, and fiduciary* – are presented. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as non-major funds.

NOTES TO THE FINANCIAL STATEMENTS

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Non-operating revenues, such as subsidies and investment earnings, result from non-exchange transactions or ancillary activities.

The City reports the following major governmental funds:

General Fund – The General Fund is the general operating fund of the City. The General Fund accounts for all financial resources except those that are required to be accounted for in another fund. The primary revenue sources are ad valorem taxes, State grants, and various other taxes and licenses. The primary expenditures are for public safety, street maintenance and construction, sanitation services, parks and recreation, and economic development.

Capital Projects Fund - Capital projects funds account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary and trust funds). North Carolina General Statutes require the establishment of a capital project fund to account for the proceeds of each bond order or order authorizing any debt instrument and for all other resources used for the capital projects financed by the bond or debt instrument proceeds.

The City reports the following non-major governmental fund:

Special Revenue Fund - Special revenue funds account for specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to expenditures for specified purposes. The City maintains one Special Revenue Fund, a Community Development Fund.

The City reports the following major enterprise funds: **Water and Sewer Fund** – used to account for the City’s water and sewer operations, and the **Mass Transit Fund** – used to account for the City’s mass transit system operations.

The City reports the following other fund types:

Internal Service Funds – Internal service funds are used to account for the financing of goods or services provided by an activity to other departments or funds on a cost-reimbursement basis. The City has two Internal Service Funds: the Workers’ Compensation Fund and the Employee Health Care Fund. The City’s internal service funds are presented in the proprietary fund financial statements. Because the principal user of the internal service fund is the General Fund, the financial statements of the internal service funds are consolidated into the governmental column when presented in the government-wide financial statements. To the extent possible, the cost of these services is reported in the appropriate functional activity (general government, public safety, transportation, etc.).

Fiduciary Funds – Fiduciary funds are used to report assets held in a trustee or agency capacity for others and therefore are not available to support City programs. The reporting focus is on net assets and changes in net assets which are reported using accounting principles similar to proprietary funds. The City’s fiduciary funds are presented in the fiduciary fund financial statements by type (pension trust fund and agency). Since by definition these assets are being held for the benefit of third parties and cannot be used to address activities or obligations of the government, these funds are not incorporated into the government-wide statements. The City’s Fiduciary Funds consist of one Pension Trust Fund and three Agency Funds. The Pension Trust Fund is used to account for the Law Enforcement Officers’ Separation Allowance, a single-employer public employee retirement system for the City’s law enforcement officers. The Agency Funds are the Boards and Commissions Fund, the Municipal Service District Fund, and the Town of East Spencer Utilities Fund.

C. Measurement Focus, Basis of Accounting, and Basis of Presentation

In accordance with North Carolina General Statutes, all funds of the City are maintained during the year using the modified accrual basis of accounting.

NOTES TO THE FINANCIAL STATEMENTS

Government-wide and Proprietary Fund Financial Statements – The government-wide, proprietary, and fiduciary fund financial statements are reported using the economic resources measurement focus. The government-wide, proprietary, and fiduciary fund financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time the liabilities are incurred, regardless of when the related cash flows take place. Non-exchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value, include property taxes, grants, and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

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

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 a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise funds are charges to customers for sales and services. The City also recognizes as operating revenue tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Governmental Fund Financial Statements – Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

The City considers all revenues available if they are collected within 90 days after year-end, except for property taxes. Ad valorem taxes receivable are not accrued as a revenue because the amount is not susceptible to accrual. At June 30, taxes receivable are materially past due and are not considered to be an available resource to finance the operations of the current year. Also, as of January 1, 1993, State law altered the procedures for the assessment and collection of property taxes on registered motor vehicles in North Carolina. Effective with this change in the law, Rowan County is responsible for billing and collecting the property taxes on registered vehicles on behalf of all municipalities and special tax districts in the county, including the City of Salisbury. For motor vehicles registered under the staggered system, property taxes are due the first day of the fourth month after the vehicles are registered. The billed taxes are applicable to the fiscal year in which they become due. Therefore, the City's vehicle taxes for vehicles registered in Rowan County from March 2005 through February 2006 apply to the fiscal year ended June 30, 2006. Uncollected taxes that were billed during this period are shown as a receivable in these financial statements and are offset by deferred revenues. For vehicles registered under the annual system, taxes are due on May 1 of each year. In addition, as of January 1, 2006, State law implemented a staggered expiration date system for annually registered vehicles as part of the conversion into the staggered registration. Originally, annually registration expired December 31st each year with taxes due by May 1st of the following year. To transition from the staggered into the annual registration, the initial 2006 registration renewals will vary from 7 to 18 months after December 31, 2005. Once these initial renewals have expired, all vehicles that were previously annually registered will be in the staggered system.

Sales taxes and certain intergovernmental revenues, such as the utilities franchise tax, collected and held by the State at year-end on behalf of the City are recognized as revenue. Intergovernmental revenues and sales and services are not susceptible to accrual because generally they are not measurable until received in cash. Grant revenues which are unearned at year-end are recorded as deferred revenues.

NOTES TO THE FINANCIAL STATEMENTS

As permitted by accounting principles generally accepted in the United States of America, the City has elected to apply only applicable FASB Statements and Interpretations issued on or before November 30, 1989 that do not contradict GASB pronouncements in its accounting and reporting practices for its general government and enterprise funds.

D. Budgetary Data

The City's budgets are adopted as required by the North Carolina General Statutes. An annual budget ordinance is adopted for the General, Special Revenue, and Enterprise funds. All annual appropriations lapse at fiscal year end. Project ordinances are adopted for the Capital Project Fund and Enterprise Fund Capital Projects Fund, which are consolidated with the operating funds for reporting purposes. These appropriations continue until the project is completed. All budgets are prepared using the modified accrual basis of accounting. Expenditures may not legally exceed appropriations at the functional level for all annually budgeted funds and at the object level for the multi-year funds. Amendments are required for any revisions that alter total expenditures of any fund. All amendments must be approved by the City Council. During the year, several amendments to the original budget were necessary. The budget ordinance must be adopted by July 1 of the fiscal year or the City Council must adopt an interim budget that covers that time until the annual ordinance can be adopted.

E. Assets, Liabilities and Fund Equity

1. Deposits and Investments

All deposits of the City and of Downtown Salisbury, Inc. are made in board-designated official depositories and are secured as required by State law [G.S. 159-31]. The City and Downtown Salisbury, Inc. may designate, as an official depository, any bank or savings association whose principal office is located in North Carolina. Also, the City and Downtown Salisbury, Inc. may establish time deposit accounts such as NOW and SuperNOW accounts, money market accounts, and certificates of deposit.

State law [G.S. 159-30(c)] authorizes the City and Downtown Salisbury, Inc. to invest in obligations of the United States or obligations fully guaranteed, both as to principal and interest by the United States; obligations of the State of North Carolina; bonds and notes of any North Carolina local government or public authority; obligations of certain non-guaranteed federal agencies; certain high quality issues of commercial paper and bankers' acceptances and the North Carolina Capital Management Trust (NCCMT).

The City and Downtown Salisbury, Inc.'s investments with a maturity of more than one year at acquisition and non-money market investments are reported at fair value as determined by quoted market prices. The securities of the NCCMT Cash Portfolio, a SEC-registered (2a7) money market mutual fund, are valued at fair value, which is the NCCMT's share price. Money market investments that have a remaining maturity at the time of purchase of one year or less are reported at amortized cost. Non-participating interest earnings investment contracts are reported at cost.

2. Cash and Cash Equivalents

The City pools money from several funds to facilitate disbursement and investment and to maximize investment income. Therefore, all cash and investments are essentially demand deposits and are considered cash and cash equivalents. Downtown Salisbury, Inc. considers all highly liquid investments with a maturity of three months or less when purchased to be cash and cash equivalents.

3. Restricted Assets

The unexpended debt proceeds of the Capital Projects Fund are classified as restricted assets in the Statement of Net Assets because their use is completely restricted for the purpose for which the debt was originally issued.

NOTES TO THE FINANCIAL STATEMENTS

4. Ad Valorem Taxes Receivable

In accordance with State law [G.S. 105-347 and G.S. 159-13(a)], the City levies ad valorem taxes on property other than motor vehicles on July 1, the beginning of the fiscal year. The taxes are due on September 1 (lien date); however, interest does not accrue until the following January 6. These taxes are based on the assessed values of January 1, 2005. As allowed by State law, the City has established a schedule of discounts that apply to taxes that are paid prior to the due date. In the City's General Fund, ad valorem tax revenues are reported net of such discounts.

5. Allowances for Doubtful Accounts

All receivables that historically experience uncollectible accounts are shown net of an allowance for doubtful accounts. This amount is estimated by analyzing the percentage of receivables that were written off in prior years.

6. Inventories and Prepaid Items

The inventories of the City are valued at cost (first-in, first-out), which approximates market. The City's General Fund inventory consists of parts used to maintain the City's vehicles.

The inventories of the City's Water and Sewer Fund consist of materials and supplies held for subsequent use. The inventories are valued at cost, on a first-in, first-out basis, which approximates market. The costs of these inventories are recorded as expenditures when used rather than when purchased. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements and expensed as the items are used.

7. Capital Assets

Capital assets are defined by the City as assets with an initial, individual cost of more than a certain amount and an estimated useful life in excess of two years. Minimum capitalization costs are as follows: buildings, \$10,000; furniture and equipment, \$5,000; infrastructure, \$100,000; and improvements other than buildings or infrastructure, \$5,000. All land is recorded as a capital asset without regard to any significant value. Purchased or constructed capital assets are reported at cost or estimated historical cost. Donated capital assets are recorded at their fair value at the date of donation. General infrastructure assets acquired prior to July 1, 2002 consist of the road network and water and sewer system assets that were acquired or that received substantial improvements subsequent to July 1, 1980, and are reported at estimated historical cost using deflated replacement cost. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Useful Lives</u>
Infrastructure	25
Buildings	40
Improvements	40
Vehicles	5
Furniture and equipment	10
Computer equipment	3

Property, plant, and equipment of Downtown Salisbury, Inc. are depreciated over their useful lives on a straight-line basis as follows:

<u>Asset Class</u>	<u>Useful Lives</u>
Furniture and equipment	10

NOTES TO THE FINANCIAL STATEMENTS

8. Long-Term Obligations

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

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

9. Compensated Absences

The vacation policy of the City provides for the accumulation of earned vacation leave as follows: police officers, 470 hours; firefighters, 582 hours; and all other employees, 360 hours. Vacation leave for the City is fully vested when earned. For the City's government-wide and proprietary funds, an expense and a liability for compensated absences and the salary-related payments are recorded as the leave is earned. The portion of that time that is estimated to be used in the next fiscal year has been included as a current liability in the government-wide and fund financial statements.

The City's sick leave policy provides for an unlimited accumulation of earned sick leave. Sick leave does not vest, but any unused sick leave accumulated at the time of retirement may be used in the determination of length of service for retirement benefit purposes. Since the City has no obligation for the accumulated sick leave until it is actually taken, no accrual for sick leave has been made.

The City's liabilities for compensated absences in the governmental funds are liquidated from the General Fund and the liabilities of the enterprise funds are liquidated from the Water and Sewer Fund and the Mass Transit Fund.

10. Net Assets/Fund Balances

Net assets in government-wide and proprietary fund financial statements are classified as invested in capital assets, net of related debt; restricted; and unrestricted. Invested in capital assets, net of related debt, represents the portion of net assets associated with non-liquid assets less the outstanding capital asset related debt. Restricted net assets represent constraints on resources that are either internally imposed by City Council for future capital projects or externally imposed by creditors, grantors, contributors, or laws or regulations of other governments; or imposed by law through state statute.

In the governmental fund financial statements, reservations of fund balance represent amounts that cannot be appropriated or are legally segregated for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

State law [G.S. 159-13(b)(16)] restricts appropriation of fund balance for the subsequent year's budget to an amount not to exceed the sum of cash and investments minus the sum of liabilities, encumbrances, and deferred revenues arising from cash receipts as those amounts stand at the close of the fiscal year preceding the budget year.

The governmental fund types classify fund balances as follows:

Reserved:

Reserved by State statute - portion of fund balance, in addition to reserves for encumbrances, which is not available for appropriation under State law [G.S. 159-8(a)]. This amount is usually comprised of accounts receivable and due from other governments that have not been offset by deferred revenues.

NOTES TO THE FINANCIAL STATEMENTS

Reserved for encumbrances - portion of fund balance available to pay for commitments related to purchase orders or contracts that remain unperformed at year-end.

Reserved for inventories – a portion of fund balance that is not available for appropriation because it represents the year-end fund balance of ending inventories, which are not expendable, available resources.

Reserved for prepaid items - portion of total fund balance that has been expended for the benefit of future periods.

Unreserved:

Undesignated – portion of total fund balance available for appropriation that is uncommitted at year-end.

F. Revenues, Expenditures, and Expenses

1. Grant Revenue

The City recognizes grant revenue when all applicable eligibility requirements, including time requirements, are met. Resources transmitted to the City before the eligibility requirements have been met are recorded and reported as deferred revenues.

2. Investment Income

The City recognizes investment income from pooled cash and investments as revenues in the individual funds based on the percentage of a fund's average monthly investment in pooled cash and investments to the total average monthly investment in pooled cash and investments. All investment earnings are allocated and recorded monthly in each individual fund.

3. Inter-fund Transactions

Inter-fund transactions are either for services provided or transfers. Services that are deemed to be reasonably equivalent in value are treated as revenues and expenditures/expenses. Reimbursements occur when one fund incurs the cost, and then charges the appropriate benefited fund and reduces its related cost as a reimbursement, if material. Transfers within governmental activities and business-type activities are eliminated upon consolidation.

G. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

Note 2. Detail Notes On All Funds

A. Assets

1. Deposits

All deposits of the City and Downtown Salisbury, Inc. are either insured or collateralized by using one of two methods. Under the Dedicated Method, all deposits that exceed the federal depository insurance coverage level are collateralized with securities held by the City's and component units' agents in these units' names. Under the Pooling Method, which is a collateral pool, all uninsured deposits are collateralized with securities held by the State Treasurer's agent in the name of the State Treasurer. Since the State Treasurer is acting in a fiduciary capacity for the City and the component unit, these deposits are considered to be held by the City's and the components' agent in their names. The amount of the pledged collateral is based on an approved averaging method for non-interest bearing deposits and the actual current balance for interest bearing deposits. Depositories using the Pooling Method

NOTES TO THE FINANCIAL STATEMENTS

report to the State Treasurer the adequacy of their pooled collateral covering uninsured deposits. The State Treasurer does not confirm this information with the City or the escrow agent. Because of the inability to measure the exact amount of collateral pledged for the City or its component unit under the Pooling Method, the potential exists for under-collateralization, and this risk may increase in periods of high cash flows. However, the State Treasurer of North Carolina enforces strict standards of financial stability for each depository that collateralizes public deposits under the Pooling Method. The City has deposits in banks utilizing both the Dedicated Method and the Pooling Method. The City has no policy regarding custodial credit risk for deposits.

At June 30, 2006, the City's deposits had a carrying amount of \$8,847,372 and a bank balance of \$9,444,411. Of the bank balance, \$707,308 was covered by federal depository insurance and the remainder was covered by collateral held under either the Dedicated Method or the Pooling Method. At June 30, 2006, the City's petty cash fund totaled \$3,065.

2. Investments

At June 30, 2006, the City's investment balances were as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturity</u>	<u>Rating</u>
GE Capital Commercial Paper	\$ 1,944,183	29-Dec-06	A1+, P1
Merrill Lynch Commercial Paper	1,938,560	23-Jan-07	A-1, P-1, F1+
NC Capital Management Trust-Cash Portfolio	<u>5,382,194</u>	N/A	AAAm
Total	<u>\$ 9,264,937</u>		

Interest Rate Risk – As a means of limiting its exposure to fair value losses arising from rising interest rates, the City limits its investment portfolio to maturities of less than 12 months. The City has no formal policy regarding interest rate risk.

Credit Risk – The City has no policy regarding credit risk. The City's investment in the NC Capital Management Trust Cash Portfolio carried a credit rating of AAAM by Standard & Poor's as of June 30, 2006. The City's investment in GE Capital Commercial Paper has been rated A1+ by Moody's Investors Service and P1 by Standard and Poor's. The City's investment in Merrill Lynch Commercial Paper has been rated A1 by Moody's Investors Service, P1 by Standard and Poor's, and F1+ by Fitch Ratings.

Concentration of Credit Risk – The City places no limit on the amount that the City may invest in any one issuer. More than five percent of the City's investments are in the Federal Home Loan Bank Discount Note (18.9%), the American General Finance Commercial Paper (21%), and the Goldman Sachs Commercial Paper (21%).

3. Receivables - Allowances for Doubtful Accounts

The amounts shown in the statement of net assets for receivables are net of the following allowances for doubtful accounts.

<u>Fund</u>	<u>June 30, 2006</u>
General Fund:	
Taxes receivable	<u>\$ 230,000</u>
Enterprise Funds:	
Utility receivables	<u>\$ 60,000</u>

NOTES TO THE FINANCIAL STATEMENTS

4. Capital Assets

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

	<u>Balances</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balances</u>
Governmental activities:				
Capital assets not being depreciated:				
Land	\$ 3,157,445	\$ 205,201	\$ -	\$ 3,362,646
Construction in progress	415,161	2,917,306	100,350	3,232,117
Total capital assets not being depreciated	<u>\$ 3,572,606</u>	<u>\$ 3,122,507</u>	<u>\$ 100,350</u>	<u>\$ 6,594,763</u>
Capital assets being depreciated:				
Buildings	\$ 2,307,684	\$ -	\$ -	\$ 2,307,684
Other improvements	10,579,980	100,350	5,752	10,674,578
Equipment	5,688,389	217,613	77,364	5,828,638
Vehicles and motorized equipment	10,322,882	1,085,341	530,288	10,877,935
Infrastructure	32,447,486	1,706,500	-	34,153,986
Total capital assets being depreciated	<u>\$ 61,346,421</u>	<u>\$ 3,109,804</u>	<u>\$ 613,404</u>	<u>\$ 63,842,821</u>
Less accumulated depreciation for:				
Buildings	\$ 1,006,796	\$ 62,160	\$ -	\$ 1,068,956
Other improvements	3,030,670	187,771	5,752	3,212,689
Equipment	3,503,272	755,056	77,366	4,180,962
Vehicles and motorized equipment	8,570,339	628,257	524,491	8,674,105
Infrastructure	10,728,567	1,129,890	-	11,858,457
Total accumulated depreciation	<u>\$ 26,839,644</u>	<u>\$ 2,763,134</u>	<u>\$ 607,609</u>	<u>\$ 28,995,169</u>
Total capital assets being depreciated, net	<u>\$ 34,506,777</u>	<u>\$ 346,670</u>	<u>\$ 5,795</u>	<u>\$ 34,847,652</u>
Governmental activity capital assets, net	<u><u>\$ 38,079,383</u></u>	<u><u>\$ 3,469,177</u></u>	<u><u>\$ 106,145</u></u>	<u><u>\$ 41,442,415</u></u>

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

General government	\$ 834,735
Public safety	368,158
Transportation	1,277,956
Environmental protection	119,520
Cultural and recreational	133,231
Land management and development	29,534
Total depreciation expense	<u><u>\$ 2,763,134</u></u>

NOTES TO THE FINANCIAL STATEMENTS

	Beginning Balances	Increases	Decreases	Ending Balances
Business-type activities				
Water and Sewer Fund				
Capital assets not being depreciated:				
Land	\$ 2,072,067	\$ -	\$ -	\$ 2,072,067
Construction in progress	4,535,599	1,508,133	5,223,021	820,711
Total capital assets not being depreciated	<u>\$ 6,607,666</u>	<u>\$ 1,508,133</u>	<u>\$ 5,223,021</u>	<u>\$ 2,892,778</u>
Capital assets being depreciated:				
Plant and distribution systems	\$ 149,982,029	\$ 5,494,611	\$ -	\$ 155,476,640
Furniture and maintenance equipment	2,817,424	72,133	21,027	2,868,530
Vehicles and motorized equipment	3,626,066	297,509	33,829	3,889,746
Total capital assets being depreciated	<u>\$ 156,425,519</u>	<u>\$ 5,864,253</u>	<u>\$ 54,856</u>	<u>\$ 162,234,916</u>
Less accumulated depreciation for:				
Plant and distribution systems	\$ 39,402,051	\$ 3,771,624	\$ -	\$ 43,173,675
Furniture and maintenance equipment	2,366,100	245,350	21,027	2,590,423
Vehicles and motorized equipment	2,587,631	317,644	33,829	2,871,446
Total accumulated depreciation	<u>\$ 44,355,782</u>	<u>\$ 4,334,618</u>	<u>\$ 54,856</u>	<u>\$ 48,635,544</u>
Total capital assets being depreciated, net	<u>\$ 112,069,737</u>	<u>\$ 1,529,635</u>	<u>\$ -</u>	<u>\$ 113,599,372</u>
Water and Sewer Fund capital assets, net	<u>\$ 118,677,403</u>	<u>\$ 3,037,768</u>	<u>\$ 5,223,021</u>	<u>\$ 116,492,150</u>
Transit Fund				
Capital assets being depreciated:				
Buildings and improvements	\$ 467,924	\$ -	\$ -	\$ 467,924
Furniture and maintenance equipment	29,057	-	-	29,057
Vehicles and motorized equipment	1,775,516	34,366	17,348	1,792,534
Total capital assets being depreciated	<u>\$ 2,272,497</u>	<u>\$ 34,366</u>	<u>\$ 17,348</u>	<u>\$ 2,289,515</u>
Less accumulated depreciation for:				
Buildings and improvements	\$ 467,924	\$ -	\$ -	\$ 467,924
Furniture and maintenance equipment	26,521	2,536	-	29,057
Vehicles and motorized equipment	769,537	229,487	17,348	981,676
	<u>\$ 1,263,982</u>	<u>\$ 232,023</u>	<u>\$ 17,348</u>	<u>\$ 1,478,657</u>
Transit Fund capital assets, net	<u>\$ 1,008,515</u>	<u>\$ (197,657)</u>	<u>\$ -</u>	<u>\$ 810,858</u>
Business-type activities capital assets, net	<u>\$ 119,685,918</u>	<u>\$ 2,840,111</u>	<u>\$ 5,223,021</u>	<u>\$ 117,303,008</u>

Construction commitments

The City has active construction projects as of June 30, 2006. At year-end, the City's commitments with contractors are as follows:

Project	Spent-to-date	Remaining Commitment
Public Safety Facilities	<u>\$ 2,530,773</u>	<u>\$ 1,432,990</u>

NOTES TO THE FINANCIAL STATEMENTS

B. Liabilities

1. Pension Plan Obligations

a. Local Governmental Employees' Retirement System

Plan Description. The City of Salisbury contributes to the statewide Local Governmental Employees' Retirement System (LGERS), a cost-sharing multiple-employer defined benefit pension plan administered by the State of North Carolina. LGERS provides retirement and disability benefits to plan members and beneficiaries. Article 3 of G.S. Chapter 128 assigns the authority to establish and amend benefit provisions to the North Carolina General Assembly. The Local Governmental Employees' Retirement System is included in the Comprehensive Annual Financial Report (CAFR) for the State of North Carolina. The State's CAFR includes financial statements and required supplementary information for LGERS. That report may be obtained by writing to the Office of the State Controller, 1410 Mail Service Center, Raleigh, North Carolina 27699-1410, or by calling (919) 981-5454.

Funding Policy. Plan members are required to contribute six percent of their annual covered salary. The City is required to contribute at an actuarially determined rate. For the City, the current rate for employees not engaged in law enforcement and for law enforcement officers is 4.80% and 4.64%, respectively, of annual covered payroll. The contribution requirements of members and of the City of Salisbury are established and may be amended by the North Carolina General Assembly. The City's contributions to LGERS for the years ended June 30, 2006, 2005, and 2004 were 797,786, 766,837, and \$714,372, respectively. The contributions made by the City equaled the required contributions for each year.

b. Law Enforcement Officers' Special Separation Allowance

1. Plan Description

The City administers a public employee retirement system (the "Separation Allowance"), a single-employer defined benefit pension plan that provides retirement benefits to the City's qualified sworn law enforcement officers. The Separation Allowance is equal to .85 percent of the annual equivalent of the base rate of compensation most recently applicable to the officer for each year of creditable service. The retirement benefits are not subject to any increases in salary or retirement allowances that may be authorized by the North Carolina General Assembly. Article 12D of G.S. Chapter 143 assigns the authority to establish and amend benefit provisions to the General Assembly. The Separation Allowance does not issue separate audited financial statements, but is included in the Comprehensive Annual Financial Report (CAFR) of the City of Salisbury. The City's CAFR includes financial statements and required supplementary information for the Separation Allowance.

All full-time City law enforcement officers are covered by the Separation Allowance. At December 31, 2006, the Separation Allowance's membership consisted of:

Retirees and beneficiaries currently receiving benefits	2
Terminated plan members entitled to but not yet receiving benefits	-
Active plan members	<u>79</u>
Total	<u>81</u>

2. Summary of Significant Accounting Policies

Basis of Accounting. Financial statements for the Separation Allowance are prepared using the accrual basis of accounting. Employer contributions to the plan are recognized when due and when the City has made a formal commitment to provide the contributions. Benefits are recognized when due and payable in accordance with the terms of the plan.

NOTES TO THE FINANCIAL STATEMENTS

Method Used to Value Investments. As noted in Note 1E previously, cash and investments are held in a single central depository with each fund owning a pro-rata share. Therefore, cash and investments are essentially demand deposits and are considered to be cash and cash equivalents. Investments are reported at cost which approximates market.

3. Contributions

North Carolina statutes require the City to provide these retirement benefits. The City has chosen to fund the amounts necessary to cover the benefits earned by making contributions based on actuarial valuations. For the current year, the City contributed \$108,259, or 3.56% of annual covered payroll. There were no contributions made by employees. The City's obligation to contribute to this plan is established and may be amended by the North Carolina General Assembly. Administration costs of the Separation Allowance are paid by the General Fund.

The annual required contribution for the current year was determined as part of the December 31, 2005 actuarial valuation using the projected unit credit actuarial cost method. The actuarial assumptions included (a) 7.25% investment rate of return (net of administrative expenses) and (b) projected salary increases ranging from 4.5% to 12.3% per year. Item (b) included an inflation adjustment of 3.75%. The assumptions did not include postretirement benefit increases. The actuarial value of assets was determined using the market value of investments. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payrolls on a closed basis. The remaining amortization period at December 31, 2005 was 25 years.

4. Annual Pension Cost and Net Pension Asset

The City's annual pension cost and net pension asset to the Separation Allowance for the current year were as follows:

Annual required contribution	\$ 100,962
Interest on net pension obligation	(2,377)
Adjustment to annual required contribution	<u>1,883</u>
Annual pension cost	\$ 100,468
Contributions made	<u>108,259</u>
Decrease in net pension asset	\$ 7,791
Net pension asset beginning of year	<u>32,780</u>
Net pension asset end of year	<u><u>\$ 40,571</u></u>

<u>Fiscal Year</u> <u>Ended</u>	<u>Annual Pension</u> <u>Cost (APC)</u>	<u>Percentage of</u> <u>APC Contributed</u>	<u>Net Pension</u> <u>Asset</u>
6/30/2006	\$100,468	107.75%	\$40,571
6/30/2005	103,619	100.20%	32,780
6/30/2004	87,132	100.70%	32,578

c. Supplemental Retirement Income Plan

Plan Description: The City contributes to the Supplemental Retirement Income Plan (Plan), a defined contribution pension plan administered by the Department of State Treasurer and a Board of Trustees. The Plan provides retirement benefits to all full-time employees of the City. Article 5 of G.S. Chapter 135 assigns the authority to establish and amend benefit provisions to the North Carolina General Assembly.

Funding Policy: Article 12E of G.S. Chapter 143 requires the City to contribute each month an amount equal to 5 percent of each law enforcement officer's salary. In addition to this requirement, the City has elected to contribute to the Plan an amount equal to 2 percent of the monthly salary of

NOTES TO THE FINANCIAL STATEMENTS

each employee not engaged in law enforcement. All amounts contributed are vested immediately. Also, employees may make voluntary contributions to the plan. Contributions for the year ended June 30, 2006 were \$732,450, which consisted of \$430,739 from the City and \$301,711 from the employees.

d. Firemen's and Rescue Squad Workers' Pension Fund

Plan Description: The State of North Carolina contributes, on behalf of the City of Salisbury, to the Firemen's and Rescue Squad Workers' Pension Fund (Fund), a cost-sharing multiple-employer defined benefit pension plan with a special funding situation administered by the State of North Carolina. The fund provides pension benefits for eligible fire and rescue squad workers that have elected to become members of the Fund. Article 86 of G.S. Chapter 58 assigns the authority to establish and amend benefit provisions to the North Carolina General Assembly. The Firemen's and Rescue Squad Workers' Pension Fund is included in the Comprehensive Annual Financial Report (CAFR) for the State of North Carolina. The State's CAFR includes financial statements and required supplementary information for the fund. That report may be obtained by writing to the Office of the State Controller, 1410 Mail Service Center, Raleigh, North Carolina 27699-1410, or by calling (919) 981-5454.

Funding Policy: Plan members are required to contribute \$10 per month to the Fund. The State, a non-employer contributor, funds the plan through appropriations. The City does not contribute to the Fund. Contribution requirements of plan members and the State of North Carolina are established and may be amended by the North Carolina General Assembly.

For the fiscal year ended June 30, 2006, the City has recognized on-behalf payments for pension contributions made by the state as a revenue and an expenditure of \$15,891 for the 73 employed firemen who perform firefighting duties for the City's fire department.

e. Other Post-employment Benefits

The City provides post-employment health care benefits to retirees of the City, provided they participate in the North Carolina Local Governmental Employees' Retirement System (System), qualify for unreduced retirement benefits from the System, and have at least 15 years of creditable service with the City. The City pays the full cost of coverage for these benefits. Also, the City's retirees can purchase coverage for their dependents at the City's group rates. Currently, twenty retirees are eligible for post-employment health benefits. For the fiscal year ended June 30, 2006, the City made payments for post-employment health benefit premiums of \$130,774. The City is self-insured for employee and retiree health care benefits.

The City of Salisbury has elected to provide death benefits to employees through the Death Benefit Plan for members of the Local Governmental Employees' Retirement System (Death Benefit Plan), a multiple-employer State-administered cost-sharing plan funded on a one-year term cost basis. The beneficiaries of those employees who die in active service after one year of contributing membership in the System, or who die within 180 days after retirement or termination of service and have at least one year of contributing membership service in the System at the time of death are eligible for death benefits. Lump sum death benefit payments to beneficiaries are equal to the employee's 12 highest months salary in a row during the 24 months prior to his/her death. Effective July 1, 2004, death benefits must be at least \$25,000 but cannot exceed \$50,000. All death benefit payments are made from the Death Benefit Plan. The City has no liability beyond the payment of monthly contributions. Contributions are determined as a percentage of monthly payrolls, based upon rates established annually by the State. Separate rates are set for employees not engaged in law enforcement and for law enforcement officers. Because the benefit payments are made by the Death Benefit Plan and not by the City, the City does not determine the number of eligible participants. For the fiscal year ended June 30, 2006, the City made contributions to the State for death benefits of \$19,355. The City's required contributions for employees not engaged in law enforcement and for law enforcement officers represented 0.11% and 0.14% of covered payroll, respectively. The contributions to the Death Benefit Plan cannot be separated between the post-employment benefit amount and the other benefit amount.

NOTES TO THE FINANCIAL STATEMENTS

2. Deferred Revenue

As discussed in Note 1C, property taxes receivable that are measurable but not available are recorded as taxes receivable and as deferred revenue. Likewise, prepaid property taxes or privilege licenses have not met the recognition criteria and are recorded as deferred revenue. Other deferred revenue in the General Fund represents grants and donations received for various downtown enhancement projects and the purchase of equipment for the police department. The balance in deferred revenue in the governmental fund statements at year end, including these items, is composed of the following elements:

	<u>General Fund</u>
Unearned	
Unspent grants and donations	\$ 380,681
Prepaid property taxes	2,469
Unavailable	
Taxes receivable, net	<u>551,631</u>
Total deferred revenue	<u>\$ 934,781</u>

3. Risk Management

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City participates in a self-funded risk financing pool administered by the North Carolina League of Municipalities. This pool provides \$1,000,000 in general liability coverage, \$3,000,000 in liability coverage for law enforcement officers, and \$3,000,000 for automobile liability. In addition, the City maintains replacement cost insurance on real and personal property, including boiler and machinery, in an amount of \$102,598,817. The City also provides coverage for employee dishonesty in the amount of \$100,000 and fidelity insurance of the Finance Director's office for \$100,000. The pool is reinsured through commercial companies for single occurrence claims against property, general liability, and auto liability in excess of \$300,000.

There have been no significant reductions in insurance coverage in the prior year, and settled claims have not exceeded coverage in any of the past three fiscal years.

In addition, the City currently self-insures an employee health benefits program through a third party administrator. However, the City's exposure is limited to \$60,000 per individual and to 120% of estimated annual aggregate claims. The City also carries an excess workers' compensation policy through a commercial insurer in the amount of \$1,000,000. The City retains a \$300,000 deductible for this coverage. Liabilities include an amount for claims that have been incurred but not reported (IBNRs). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of pay-outs, and other economic and social factors. The liability for claims is reported in the current liabilities of the internal service funds. Changes in the balances of claims liabilities during the past three years are as follows:

	<u>Year ended</u> <u>June 30, 2004</u>	<u>Year ended</u> <u>June 30, 2005</u>	<u>Year ended</u> <u>June 30, 2006</u>
Unpaid claims, beginning of fiscal year	\$ 395,460	\$ 459,130	\$ 515,003
Incurred claims (including IBNRs)	2,887,730	3,082,898	3,476,954
Claim payments	<u>(2,824,060)</u>	<u>(3,027,025)</u>	<u>(3,517,579)</u>
Unpaid claims, end of fiscal year	<u>\$ 459,130</u>	<u>\$ 515,003</u>	<u>\$ 474,378</u>

An independent review of the City's various risk management activities is conducted annually, and coverage is adjusted accordingly as needed. There have been no reductions in insurance coverage from the prior year.

NOTES TO THE FINANCIAL STATEMENTS

4. Claims, Judgments, and Contingent Liabilities

At June 30, 2006 the City was a defendant to various lawsuits. In the opinion of the City's management and the City attorney, the ultimate effect of these legal matters will not have a material adverse effect on the City's financial position.

5. Long-Term Obligations

a. Capital Leases

The City has entered into various agreements to lease certain water and sewer distribution systems. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of the future minimum lease payments as of the date of their inception. Interest rates on these agreements range from 3.385% to 5.6%. The City has recorded water and sewer assets related to these leases at their fair value of \$7,898,494. The future minimum lease payments at June 30, 2006 total \$3,506,177, including \$706,292 of interest. Upon completion of these lease payments the City will take ownership of the related assets.

The future minimum lease obligations as of June 30, 2006 were as follows:

Year Ending June 30,	Capital Leases	
	Principal	Interest
2007	\$ 264,190	\$ 115,559
2008	260,846	104,983
2009	267,585	94,605
2010	274,409	83,860
2011	276,325	72,745
2012-2016	1,246,530	205,630
2017-2021	210,000	28,910
	<u>\$ 2,799,885</u>	<u>\$ 706,292</u>

b. Installment Purchases

The City has entered into various installment purchase contracts to finance the acquisition and renovation of various equipment and facilities. These installment purchase contracts are outlined as follows:

Installment purchase contract for capital improvements and facilities renovations from BB&T Leasing Corporation, dated December 29, 1999, payable in twenty semi-annual installments of \$63,332 at an effective interest rate of 4.73%.

Installment purchase contract from Bank of America for construction and capital improvements of facilities, dated December 22, 2000, payable in thirty semi-annual installments consisting of \$33,333 principal plus interest at an effective rate of 5.25%.

Installment purchase contract from F & M Bank for the purchase of real estate, dated February 24, 2003, payable in thirty-six monthly payments of interest only, followed by twenty-two monthly payments of \$7,372 and one final payment of all remaining principal plus accrued interest, which is due in January 2008.

Installment purchase contract from Wachovia Bank and Trust for the purchase of new telecommunications equipment, dated April 12, 2004, payable in eighteen semi-annual installments consisting of \$110,583 principal plus interest at an effective rate of 2.93%.

NOTES TO THE FINANCIAL STATEMENTS

Installment purchase contract from BB&T for the purchase of Emergency 911 telecommunications equipment, dated February 23, 2005, payable in fifty-nine monthly installments of \$3,524 at an effective interest of 3.45%.

Installment purchase contract from Bank of America for construction and improvements of City facilities dated May 5, 2006, payable in thirty semi-annual installments consisting of \$118,856 principal plus interest at 3.83%.

The future minimum payments of the installment purchases as of June 30, 2006, including \$1,504,630 of interest are as follows:

Year Ending June 30,	Governmental Activities Installment Purchases	
	Principal	Interest
2007	\$ 722,961	\$ 270,952
2008	1,611,676	228,619
2009	685,713	181,379
2010	611,803	155,203
2011	525,545	134,325
2012-2016	1,930,894	408,968
2017-2021	1,188,560	125,184
	<u>\$ 7,277,152</u>	<u>\$ 1,504,630</u>

c. General Obligation Indebtedness

The City's general obligation bonds serviced by the governmental funds were issued for the acquisition and improvement of parks and recreation facilities. Those general obligation bonds issued to finance the construction of facilities in the operations of the water and sewer system and which are being retired by its resources are reported as long-term debt in the Water and Sewer Fund. All general obligation bonds are collateralized by the full faith, credit, and taxing power of the City. Principal and interest requirements are appropriated when due.

Bonds payable at June 30, 2006 are comprised of the following individual issues:

	<u>Balance June 30, 2006</u>
Serviced by the General Fund:	
\$3,000,000 Parks and Recreation Bonds, Series 1997, average rate of 4.77%, issued December 1997, maturing serially to 2017	\$ 2,075,000
Serviced by the Water and Sewer Fund:	
\$700,000 Water Bonds, Series 1997, average rate of 4.74%, issued December 1997, maturing serially to 2008	\$ 100,000
\$3,250,000 Water Bonds, Series 1998, average rate of 4.40%, issued June 1998, maturing serially to 2017	1,850,000
\$12,100,000 Refunding Bonds, Series 2003, average rate of 3.43%, issued August 2003, maturing serially to 2015	
This amount is net of unamortized issuance cost and interest of \$887,288	<u>8,642,712</u>
Subtotal	<u>\$ 10,592,712</u>
Total General Obligation Indebtedness	<u>\$ 12,667,712</u>

NOTES TO THE FINANCIAL STATEMENTS

Annual debt service requirements to maturity for general obligation indebtedness are as follows:

Year Ending June 30,	Governmental Activities		Business-Type Activities	
	Principal	Interest	Principal	Interest
2007	\$ 200,000	\$ 99,550	\$ 1,405,000	\$ 401,052
2008	200,000	90,050	1,330,000	360,915
2009	200,000	80,550	1,265,000	318,128
2010	200,000	70,950	1,245,000	277,728
2011	200,000	61,350	1,225,000	235,787
2012-2016	1,000,000	162,750	4,910,000	515,437
2017	75,000	3,750	100,000	4,500
	<u>\$ 2,075,000</u>	<u>\$ 568,950</u>	<u>\$ 11,480,000</u>	<u>\$ 2,113,547</u>

Advance Refunding

On August 12, 2003, the City issued \$12.1 million in general obligation Water and Sewer Refunding Bonds with an interest rate of 3.43% to advance refund \$11.9 million of outstanding Water and Sewer Funds with interest rates ranging from 5.28% to 6.52%. The net proceeds of \$11.9 million were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refunded bonds. As a result, as of August 12, 2003, the refunded bonds were considered to be defeased and the liabilities for those bonds were removed from the Water and Sewer Fund.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$1,183,050. This difference represents bond issuance cost of \$157,772 and the present value of future interest payments to be made by the escrow agent. This difference is reported in the accompanying financial statements, net of the current year's amortization of \$98,587, as a deduction from bonds payable and is being charged to operations through the year 2015, the life of the new debt, which is shorter than the life of the refunded debt, using the straight-line method which approximates the effective-interest method. The City completed the advance refunding to reduce its total debt service payments over twelve years by \$352,806 and to obtain an economic gain (difference between the present values of the old and the new debt service payments) of \$309,359.

d. State Bond Loans

The long-term debt of the City's Enterprise Funds includes the following State Clean Water Bond Loans in the Water and Sewer Fund:

	Balance <u>June 30, 2006</u>
\$5,000,000 State Bond Loan, average rate of 3.43%, issued November 1997 maturing serially to 2017	\$ 2,750,000
\$450,120 State Bond Loan, average rate of 3.43%, issued November 1997 maturing serially to 2017	247,566
\$3,000,000 State Bond Loan, average rate of 2.60%, issued November 1999 maturing serially to 2019	2,100,000
\$9,200,000 State Bond Loan, average rate of 2.60%, issued June 2000 maturing serially to 2020	<u>6,440,000</u>
Total State Bond Loans	<u>\$ 11,537,566</u>

NOTES TO THE FINANCIAL STATEMENTS

Annual debt service requirements to maturity for the City's State Bond Loans are as follows:

Year Ending June 30,	Business-Type Activities	
	State Bond Loans	
	Principal	Interest
2007	\$ 882,506	\$ 324,857
2008	882,506	299,650
2009	882,506	274,443
2010	882,506	249,236
2011	882,506	224,029
2012-2016	4,412,530	742,037
2017-2020	2,712,506	167,947
	<u>\$ 11,537,566</u>	<u>\$ 2,282,199</u>

e. Revenue Bonds

The long-term debt of the City's Enterprise Funds includes Revenue Bonds in the Water and Sewer Fund where the City pledges income derived from the Enterprise Fund acquiring on constructing assets with the proceeds to pay debt service. Revenue bonds in the Water and Sewer Fund consist of the following issues:

	Balance <u>June 30, 2006</u>
\$2,040,000 Water and Sewer Revenue Bonds, Series 1998, average rate of 4.78%, issued January 1998, maturing serially to 2018	\$ 1,435,000
\$20,505,000 Water and Sewer Revenue Bonds, Series 2002, average rate of 3.66%, issued May 2002, maturing serially to 2027	
The amount is net of unamortized issuance costs of \$440,761	<u>18,339,239</u>
Total Revenue Bonds	<u>\$ 19,774,239</u>

The future payments of the revenue bonds are as follows:

June 30,	Principal	Interest
2007	\$ 650,000	\$ 958,331
2008	675,000	934,226
2009	700,000	907,728
2010	730,000	879,336
2011	760,000	929,101
2012-2016	4,360,000	3,677,037
2017-2021	4,985,000	2,574,929
2022-2026	5,975,000	1,270,500
2027	1,380,000	69,000
	<u>\$ 20,215,000</u>	<u>\$ 12,200,188</u>

The Revenue Bond General Trust Indenture requires that the City must maintain certain debt covenants relating to reporting requirements, annual budgets, and minimum utility funds revenues. Net revenues available for revenue bond debt service cannot be less than one hundred twenty percent (120%) of the long-term debt service requirement for parity indebtedness. The City has been in compliance with these covenants since the issuance of the Revenue Bonds. The calculations of the City's revenue bond coverage for the last three years are as follows:

NOTES TO THE FINANCIAL STATEMENTS

Fiscal Year	Gross Revenues (1)	Operating Expenditures(2)	Net Revenues Available for Revenue Bond Debt Service	Debt Service Requirements (3)			Coverage
				Principal	Interest	Total	
2004	\$ 16,218,662	\$ 10,696,926	\$ 5,521,736	\$ 1,472,506	\$ 1,420,340	\$ 2,892,846	190.88%
2005	16,841,357	10,952,357	5,889,000	1,492,506	1,375,815	2,868,321	205.31%
2006	18,132,373	11,843,353	6,289,020	630,000	980,535	1,610,535	390.49%

- (1) Total operating revenues plus investment earnings exclusive of revenue bond investment earnings.
(2) Total operating expenses exclusive of depreciation.
(3) Parity debt includes revenue bonds and State Clean Water Bonds in 2004-2005, but only revenue bonds in 2006.

f. HUD Section 108 Loan

The City borrowed funds on loan from the U. S. Department of Housing and Urban Development pursuant to Section 108 of Title I of the Community Development Act of 1974. The loan was used to renovate two buildings to form a new community center. The City borrowed a total of \$596,000 under this loan. This Section 108 loan is serviced by the City's Special Revenue Fund.

Annual debt service requirements to maturity for the City's HUD Section 108 Loan are as follows:

Year Ending June 30,	Governmental Activities HUD Section 108 Loan	
	Principal	Interest
2007	\$ 32,000	\$ 24,169
2008	32,000	23,308
2009	32,000	22,272
2010	32,000	21,099
2011	32,000	19,824
2012-2016	160,000	77,143
2017-2021	164,000	36,083
2022-2023	48,000	2,135
	<u>\$ 532,000</u>	<u>\$ 226,033</u>

g. Changes in Long-Term Liabilities

	June 30, 2005	Additions	Retirements	Change in Unamortized Costs	June 30, 2006	Current Portion of Balance
Governmental Activities						
General obligation bonds	\$ 2,265,000	\$ -	\$ 190,000	\$ -	\$ 2,075,000	\$ 200,000
Installment purchases	4,156,422	3,565,680	444,950	-	7,277,152	722,961
Section 108 loan	564,000	-	32,000	-	532,000	32,000
Compensated absences	1,569,344	977,920	806,772	-	1,740,492	435,123
	<u>\$ 8,554,766</u>	<u>\$ 4,543,600</u>	<u>\$ 1,473,722</u>	<u>\$ -</u>	<u>\$ 11,624,644</u>	<u>\$ 1,390,084</u>
Business-type activities						
General obligation bonds	\$ 11,934,124	\$ -	\$ 1,440,000	\$ 98,588	\$ 10,592,712	\$ 1,405,000
Revenue bonds	20,383,247	-	630,000	20,989	19,774,236	650,000
State loans	12,420,072	-	882,506	-	11,537,566	882,506
Capital leases	3,070,497	-	270,612	-	2,799,885	264,190
Compensated absences	363,839	221,612	183,639	-	401,812	100,452
	<u>\$ 48,171,779</u>	<u>\$ 221,612</u>	<u>\$ 3,406,757</u>	<u>\$ 119,577</u>	<u>\$ 45,106,211</u>	<u>\$ 3,302,148</u>
Total	<u>\$ 56,726,545</u>	<u>\$ 4,765,212</u>	<u>\$ 4,880,479</u>	<u>\$ 119,577</u>	<u>\$ 56,730,855</u>	<u>\$ 4,692,232</u>

NOTES TO THE FINANCIAL STATEMENTS

6. Accounts Payable

Accounts payable for the governmental activities and the business-type activities are as follows:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>
Accounts payable	\$ 1,816,642	\$ 473,160
Accrued payroll and payroll liabilities	806,365	241,103
Other accrued liabilities	<u>56,813</u>	<u>-</u>
	<u>\$ 2,679,820</u>	<u>\$ 714,263</u>

C. Interfund Balances and Activity

1. Balances Due to/from Other Funds

As of June 30, 2006, an amount of \$221,302 was due from the Capital Project Fund to the General Fund. This short-term loan was used for renovations to the Police Station and will be repaid from the project's installment purchase financing funds.

2. Transfers to/from Other Funds

Transfers during the year ended June 30, 2006, consisted of \$213,118 that was transferred from the General Fund to the Mass Transit Fund to cover the City's share of the operational expenses of the Mass Transit Fund.

Note 3. Joint Venture

The City and the members of the City's fire department each appoint two members to the five-member local board of trustees for the Firemen's Relief Fund. The State Insurance Commissioner appoints an additional member to the local board of trustees. The Firemen's Relief Fund is funded by a portion of the fire and lightning insurance premiums that insurers remit to the State. The State passes these moneys to the local board of the Firemen's Relief Fund. The funds are used to assist firefighters in various ways. The City obtains an ongoing financial benefit from the Fund for the on-behalf of payments for salaries and fringe benefits made to members of the City's fire department by the board of trustees. During the fiscal year ended June 30, 2006, the City reported revenues and expenditures for the payments of \$60,965 made through the Firemen's Relief Fund. The participating governments do not have any equity interest in the joint venture, so no equity has been reflected in the financial statements at June 30, 2006. The Firemen's Relief Fund does not issue separate audited financial statements. Instead, the local board of trustees files an annual financial report with the State Firemen's Association. This report can be obtained from the Association at Post Office Box 188, Farmville, NC 27828.

Note 4. Commitments and Contingencies

The City participates in a number of federal and State of North Carolina awards. For the fiscal year ended June 30, 2006, these awards were subject to audit in accordance with *Government Auditing Standards* and the provisions of OMB Circular A-133 and the State Single Audit Implementation Act. The amounts, if any, of expenditures which may be disallowed by the granting agencies resulting from this and other audits cannot be determined at this time, although the City expects they would be immaterial.

NOTES TO THE FINANCIAL STATEMENTS

Note 5. Pronouncements Issued But Not Yet Effective

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2006 that have effective dates that may impact future financial presentations. Management has not currently determined what, if any, impact implementation of the following statements may have on the financial statement of the City.

- GASB Statement Number 43, “Financial Reporting for Postemployment Benefit Plans Other Than Pensions Plans.”
- GASB Statement Number 45, “Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.”



Required Supplemental Financial Data



CITY OF SALISBURY, NORTH CAROLINA

LAW ENFORCEMENT OFFICERS' SPECIAL SEPARATION ALLOWANCE

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF FUNDING PROGRESS

Last Six Fiscal Years

Actuarial Valuation Date December 31,	(1) Actuarial Value of Assets	(2)	(3)	Funded Ratio (1) / (2)	(4) Annual Covered Payroll	UAAL as a Percentage of Covered Payroll (3) / (4)
		Actuarial Accrued Liability (AAL) Projected Unit Credit	Unfunded AAL (UAAL) (2) - (1)			
2005	\$ 746,287	\$ 1,220,368	\$ 474,081	61.15%	\$ 3,043,907	15.57%
2004	636,417	1,214,344	577,927	52.41%	2,940,751	19.65%
2003	543,886	1,185,007	641,121	45.90%	2,980,664	21.51%
2002	462,990	982,204	519,214	47.14%	2,715,519	19.12%
2001	382,392	944,593	562,201	40.48%	2,958,255	19.00%
2000	315,640	862,184	546,544	36.61%	2,793,421	19.57%

CITY OF SALISBURY, NORTH CAROLINA
LAW ENFORCEMENT OFFICERS' SPECIAL SEPARATION ALLOWANCE

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF EMPLOYER CONTRIBUTIONS

Last Six Fiscal Years

Fiscal Year Ended June 30,	Annual Required Contribution	Percentage Contributed
2006	\$ 100,962	108
2005	104,153	100
2004	87,696	101
2003	93,425	95
2002	86,797	102
2001	47,368	118

Notes to the Required Schedules:

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows.

Valuation date	12/31/2005
Actuarial cost method	Projected unit credit
Amortization method	Level percent of pay closed
Remaining amortization period	25 years
Asset valuation method	Market value
Actuarial assumptions	
Investment rate of return*	7.25%
Projected salary increases*	4.5% - 12.3%
* Includes inflation at	3.75%
Cost of living adjustments	N/A