

CITY OF METHUEN, MASSACHUSETTS

Annual Financial Statements

For the Year Ended June 30, 2010

TABLE OF CONTENTS

| | <u>Page</u> |
|--|-------------|
| INDEPENDENT AUDITORS' REPORT | 1 |
| MANAGEMENT'S DISCUSSION AND ANALYSIS | 3 |
| BASIC FINANCIAL STATEMENTS: | |
| Government-Wide Financial Statements: | |
| Statement of Net Assets | 15 |
| Statement of Activities | 16 |
| Governmental Funds: | |
| Balance Sheet | 18 |
| Reconciliation of Total Governmental Fund Balances to Net Assets of Governmental Activities in the Statement of Net Assets | 19 |
| Statement of Revenues, Expenditures, and Changes in Fund Balances | 20 |
| Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities | 21 |
| Statement of Revenues and Other Sources, and Expenditures and Other Uses - Budget and Actual - General Fund | 22 |
| Proprietary Funds: | |
| Statement of Net Assets | 23 |
| Statement of Revenues, Expenses, and Changes in Fund Net Assets | 24 |
| Statement of Cash Flows | 25 |
| Fiduciary Funds: | |
| Statement of Fiduciary Net Assets | 26 |
| Statement of Changes in Fiduciary Net Assets | 27 |
| Notes to Financial Statements | 28 |
| REQUIRED SUPPLEMENTARY INFORMATION: | |
| Schedule of Funding Progress | 57 |



10 New England Business Center Drive • Suite 107
Andover, MA 01810-1096
(978) 749-0005 • Fax (978) 749-0006
www.melansonheath.com

INDEPENDENT AUDITORS' REPORT

To the Mayor and City Council
City of Methuen, Massachusetts

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Methuen, Massachusetts, as of and for the year ended June 30, 2010 (except for the Methuen Contributory Retirement System, which is as of and for the year ended December 31, 2009), 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 Methuen's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Methuen as of June 30, 2010, and the respective changes in financial position and cash flows, where applicable, 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.

The management's discussion and analysis, appearing on the following pages, and the required supplementary information, appearing on page 57, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated March 7, 2011 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Melanson, Heath + Company P. C.

Andover, Massachusetts
March 7, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Methuen, we offer readers this narrative overview and analysis of the financial activities of the City of Methuen for the fiscal year ended June 30, 2010. Unless otherwise noted, all amounts are expressed in thousands.

A. OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the basic financial statements. The basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of our finances in a manner similar to a private-sector business.

The statement of net assets presents information on all assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position is improving or deteriorating.

The statement of activities presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities include general government, public safety, highways and streets, sanitation, economic development, and culture and recreation. The business-type activities include water and sewer activities.

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

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

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

An annual appropriated budget is adopted for the general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

Proprietary funds. Proprietary funds are maintained as follows:

Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Specifically, a single enterprise fund is used to account for the combined water and sewer operations.

Internal service funds are an accounting device used to accumulate and allocate costs internally among various functions. Specifically, internal service funds are used to account for self-insured employee health programs. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the business-type activities reported in the government-wide financial statements, only in more detail.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

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

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information which is required to be disclosed by accounting principles generally accepted in the United States of America.

B. FINANCIAL HIGHLIGHTS

- As of the close of the current fiscal year, the total of assets exceeded liabilities by \$ 50,458 (i.e., net assets), a change of \$ (3,592) in comparison to the prior year.
- As of the close of the current fiscal year, governmental funds reported combined ending fund balances of \$ 7,665, a change of \$ 2,076 in comparison with the prior year.
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$ 1,106 a change of \$ 1,058 in comparison with the prior year.
- Total bonds and loans payable at the close of the current fiscal year was \$ 69,203, a change of \$ (7,274) in comparison to the prior year.
- Total notes payable at the close of the current fiscal year was \$ 1,849, a change of \$ 107 in comparison to the prior year.

C. GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position.

The largest portion of net assets \$ 55,627 reflects our investment in capital assets (e.g., land, buildings, machinery and equipment); less any related debt used to acquire those assets that is still outstanding. These capital assets are used to provide services to citizens; consequently, these assets are not available for future spending. Although the investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of net assets \$ 935 represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets reflects a deficit of \$ (6,104).

The following is a summary of condensed government-wide financial data for the current and prior fiscal years.

| City of Methuen's Net Assets | | | | | | | | |
|-------------------------------------|-------------------|-----------|-------------------|-----------|---------------|-----------|------|--|
| | Governmental | | Business-Type | | Totals | | 2009 | |
| | <u>Activities</u> | | <u>Activities</u> | | <u>Totals</u> | | | |
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 | | |
| Current and other assets | \$ 19,495 | \$ 19,437 | \$ 8,683 | \$ 7,887 | \$ 28,178 | \$ 27,324 | | |
| Capital assets | 84,855 | 85,163 | 40,244 | 40,518 | 125,099 | 125,681 | | |
| Total assets | 104,350 | 104,600 | 48,927 | 48,405 | 153,277 | 153,005 | | |
| Long-term liabilities | 66,750 | 63,055 | 27,133 | 28,254 | 93,883 | 91,309 | | |
| Other liabilities | 6,880 | 6,270 | 1,756 | 1,376 | 8,636 | 7,646 | | |
| Total liabilities | 73,630 | 69,325 | 28,889 | 29,630 | 102,519 | 98,955 | | |
| Net assets: | | | | | | | | |
| Invested in capital assets, | | | | | | | | |
| net of related debt | 42,255 | 37,003 | 13,372 | 13,423 | 55,627 | 50,426 | | |
| Restricted | 935 | 873 | - | - | 935 | 873 | | |
| Unrestricted | (12,470) | (2,601) | 6,366 | 5,352 | (6,104) | 2,751 | | |
| Total net assets | \$ 30,720 | \$ 35,275 | \$ 19,738 | \$ 18,775 | \$ 50,458 | \$ 54,050 | | |

The following is a summary of condensed government-wide activities for the current and prior fiscal years.

| City of Methuen's Changes in Net Assets | | | | | | | | |
|--|-------------------|----------|-------------------|-----------|---------------|-----------|------|--|
| | Governmental | | Business-Type | | Totals | | 2009 | |
| | <u>Activities</u> | | <u>Activities</u> | | <u>Totals</u> | | | |
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 | | |
| Revenues: | | | | | | | | |
| Program revenues | | | | | | | | |
| Charges for services | \$ 9,404 | \$ 7,719 | \$ 10,703 | \$ 10,758 | \$ 20,107 | \$ 18,477 | | |
| Operating grants and contributions | 56,641 | 54,310 | 17 | 15 | 56,658 | 54,325 | | |
| Capital grants and contributions | 1,899 | 2,428 | - | - | 1,899 | 2,428 | | |
| General revenues | | | | | | | | |
| Property Taxes | 61,118 | 59,605 | - | - | 61,118 | 59,605 | | |
| Excises | 4,352 | 4,299 | - | - | 4,352 | 4,299 | | |
| Interest and Penalties | 375 | 475 | - | - | 375 | 475 | | |

(continued)

(continued)

| | Governmental Activities | | Business-Type Activities | | Totals | |
|--|----------------------------|-----------|-----------------------------|-----------|-----------|-----------|
| | 2010 | 2009 | 2010 | 2009 | 2010 | 2009 |
| Revenues: (continued) | | | | | | |
| Grants and contributions not restricted to specific programs | 12,189 | 12,632 | - | - | 12,189 | 12,632 |
| Investment income | 58 | 100 | 10 | 22 | 68 | 122 |
| Other | 1,338 ^(A) | 318 | - | - | 1,338 | 318 |
| Total revenues | 147,374 | 141,886 | 10,730 | 10,795 | 158,104 | 152,681 |
| Expenses: | | | | | | |
| General government | 13,589 | 14,228 | - | - | 13,589 | 14,228 |
| Public safety | 21,101 | 21,457 | - | - | 21,101 | 21,457 |
| Education | 101,866 | 97,134 | - | - | 101,866 | 97,134 |
| Public works | 8,918 | 9,703 | - | - | 8,918 | 9,703 |
| Sanitation | 2,440 | 2,635 | - | - | 2,440 | 2,635 |
| Health and human services | 1,313 | 1,363 | - | - | 1,313 | 1,363 |
| Culture and recreation | 1,940 | 1,516 | - | - | 1,940 | 1,516 |
| Interest and costs | 2,007 | 2,210 | - | - | 2,007 | 2,210 |
| Enterprise services | - | - | 8,522 | 8,415 | 8,522 | 8,415 |
| Total expenses | 153,174 | 150,246 | 8,522 | 8,415 | 161,696 | 158,661 |
| Change in net assets before transfers and loss | | | | | | |
| | (5,800) | (8,360) | 2,208 | 2,380 | (3,592) | (5,980) |
| Transfers in (out) | 1,245 | 1,515 | (1,245) | (1,515) | - | - |
| Change in net assets | (4,555) | (6,845) | 963 | 865 | (3,592) | (5,980) |
| Beginning net assets | 35,275 | 42,120 | 18,775 | 17,910 | 54,050 | 60,030 |
| Ending net assets | \$ 30,720 | \$ 35,275 | \$ 19,738 | \$ 18,775 | \$ 50,458 | \$ 54,050 |

(A) Includes a \$ 1,000 one-time special permit revenue received and transferred to the City's Stabilization Fund.

Governmental Activities - The City's negative result of \$ (4,555) in governmental activities is due primarily to an increase of \$ (9,594) to the City's Net OPEB Obligation. The City's conservative approach to budgeting and the careful monitoring of expenses and revenue activity throughout the fiscal year allowed the City to react to tightening budgets and changing fiscal conditions. Property tax collections continued to remain strong. The City's revenues increased by 4 percent or \$ 5,488, while expenses increased 2 percent or \$ 2,996.

The cost of all governmental activities this year was \$ 153,174 compared to \$ 150,246 last year. However, as shown in the Statement of Activities in the accompanying financial statements, the amount that our taxpayers ultimately financed for these activities through property taxes was only \$ 61,118 because

some of the cost was paid by those who directly benefited from the programs (i.e. charges for services \$ 9,404) or by other governments and organizations that subsidized certain programs with grants and contributions (i.e. operating and capital grants and contributions \$ 58,540). Overall, the City's total governmental revenues increased in current year from \$ 141,886 to \$ 147,374, principally based on increase in intergovernmental aid and charges for services. The City paid for the remaining "public benefit" portion of governmental activities with property taxes and with other revenues, such as interest and general entitlements.

The table below presents the largest activities resulting in the governmental activities net assets.

| | |
|---|-------------------|
| General fund revenues in excess of expenditures | \$ 515 |
| Transfer in to general fund for enterprise indirect costs | 1,245 |
| Nonmajor fund expenditures in excess of revenues | (214) |
| Current year capital asset additions in excess of debt issuance | 2,548 |
| Debt service in excess of depreciation | 2,900 |
| Increase in net OPEB obligation | (9,594) |
| Internal service fund loss before transfers | (3,335) |
| Other | <u>1,380</u> |
| Total | \$ <u>(4,555)</u> |

Business-type Activities - Business-type activities for the year resulted in a change in net assets of \$ 963. This change resulted primarily from unspent appropriations.

D. FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, fund accounting is used to ensure and demonstrate compliance with finance-related legal requirements.

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

The General Fund is the chief operating fund. At the end of the current fiscal year, undesignated fund balance of the General Fund was \$ 1,106, while total fund balance was \$ 2,433. Total fund balance changed by \$ 1,036 after transferring \$ 1,000 to the City's Stabilization Fund. Undesignated fund balance increased by \$ 1,058, primarily from controlling costs in attempt to rebuild reserves. Revenues increased 3.2% over prior year while expenditures

increased 0.4%. Undesignated fund balance represents 0.9% of total expenditures, while total fund balance represents 1.9% of total expenditures.

At the end of the current fiscal year, the governmental funds reported a combined fund balance of \$ 7,665 with a net change in fund balance of \$ 2,076. Included in this change in fund balance are General Fund results described in the previous paragraph and the \$ 1,000 added to the City's Stabilization Fund.

Proprietary funds. Proprietary funds include the water and sewer enterprise fund found in business-type activities reported in the government-wide financial statements, and the health insurance internal service fund, with the governmental activities on the entity-wide financial statements. Factors concerning the finances of the enterprise fund have already been addressed in the entity-wide discussion of business-type activities.

The health insurance Internal Service fund incurred a significant loss during fiscal 2010. The accrual for estimated incurred, but not yet reported costs, increased by 41% over the prior year, due to a significant increase in claims and related costs. See Note 19 to the financial statements.

E. GENERAL FUND BUDGETARY HIGHLIGHTS

The Fiscal Year 2010 budget for the City of Methuen was a reflection of the financial difficulties facing communities all across the Commonwealth of Massachusetts. We are navigating through tough economic times. All communities were burdened financially during the year, and all are struggling with local priorities and needs; Methuen was no different. In fiscal year 2010, the City of Methuen lost approximately \$ 1.7 million in local aid which accounts for 38% of our revenues. The City experienced a significant increase in health care costs along with pension and indebtedness of slightly over \$ 2 million. An additional burden was placed on the administration by our legislators to avoid any significant tax increase to our taxpayers. A monumental task was bestowed upon the administration and finance department to provide an operating budget that would meet our financial obligations and continue to maintain the excellent city services we are noted for and proud to deliver.

With such a significant loss of revenues, the City was faced with layoffs which would have devastated the work force. Early projections dictated a loss in personnel in the Fire and Police Department of approximately 60 jobs. In an unprecedented move, the unions showed solidarity and offered up 10% rescissions from their salaries and ancillary pay in a united effort to assist in balancing the budget. Along with vacant positions being eliminated, combined with the rescissions, the City was able to save \$ 2.9 million in wages. This saving proved to be a windfall in balancing the FY 2010 budget.

While the budget appeared to be in balance, an uncontrollable cost was lurking in Health Care. Our utilization was up significantly and we had 31 claimants whose

average cost was \$ 96,903 that spiked our costs by approximately \$ 3 million, with no chance of reimbursement from our stop-loss insurance. By the close of Fiscal Year 2010, our Health Insurance Claims Trust Fund was disclosing a deficit of \$ 3.3 million, the first time the health insurance trust fund had a significant deficit in twenty years. The deficit has been funded by using a combination of revenue sources from the Stabilization Fund, Tax Levy and a School Department transfer to offset their share of the deficit. However the impact of the increased health care costs would have had a profound effect on the municipal budget moving forward. In order to mitigate these costs significant modifications were made to our Health Insurance plans thus assuring us financial stability into the future.

In Methuen, we are fortunate that prudent budgeting and the ability to work within our rank and file have combined to help us manage successfully through the current fiscal year and into the next.

These are uncertain economic times, and we face special challenges. We cut the budget to accommodate recent rescissions in local aid from the state, and we are still able to maintain a stable tax rate. All of our departments are working diligently to be fiscally responsible, while still providing our citizens with the services they need and deserve.

F. CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets. Total capital assets for governmental and business-type activities at year end amounted to \$ 125,099 (net of accumulated depreciation), a change of \$ (582) from the prior year. This investment in capital assets includes land, buildings and systems, improvements, machinery and equipment, and infrastructure.

The following table provides a summary of the City's capital assets at June 30:

**City of Methuen's Capital Assets
(net of accumulated depreciation)**

| | Governmental Activities | | Business-type Activities | | Totals | |
|--------------------------------------|----------------------------|------------------|-----------------------------|------------------|-------------------|-------------------|
| | <u>2010</u> | <u>2009</u> | <u>2010</u> | <u>2009</u> | <u>2010</u> | <u>2009</u> |
| Land improvements | \$ 2,621 | \$ 2,738 | \$ 10 | \$ 12 | \$ 2,631 | 2,750 |
| Construction | 61,877 | 63,958 | 28,785 | 17,217 | 90,662 | 81,175 |
| Infrastructure | 7,112 | 6,821 | 10,019 | 10,055 | 17,131 | 16,876 |
| Machinery and equipment | 1,179 | 1,302 | 918 | 996 | 2,097 | 2,298 |
| Licensed vehicles | 1,200 | 1,085 | 260 | 110 | 1,460 | 1,195 |
| Land, easements, and right of way | 9,210 | 9,210 | 252 | 252 | 9,462 | 9,462 |
| Construction in progress | <u>1,656</u> | <u>49</u> | <u>-</u> | <u>11,876</u> | <u>1,656</u> | <u>11,925</u> |
| Total net assets | <u>\$ 84,855</u> | <u>\$ 85,163</u> | <u>\$ 40,244</u> | <u>\$ 40,518</u> | <u>\$ 125,099</u> | <u>\$ 125,681</u> |

Major capital asset acquisitions during the current fiscal year consist of the following:

| | |
|------------------------------------|--------|
| Governmental | |
| Highway improvements | \$ 853 |
| High School renovation | 1,519 |
| Dump trucks | 426 |
| Business-Type: | |
| Water treatment plant improvements | \$ 114 |
| Sewer system rehab | 225 |
| Trucks | 194 |

Additional information on capital assets can be found in footnote 11.

Long-Term Debt. At the end of the current fiscal year, total bonded debt including long-term loans outstanding was \$ 69,203, all of which was backed by the full faith and credit of the government. The City's credit rating has been downgraded to A3 for fiscal year 2010, reflecting the City's weakened financial position with minimal reserve levels and increasing personnel-driven costs.

Additional information on long-term debt can be found in the footnotes to the financial statements.

G. ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

According to economic forecasts, Fiscal Year 2011 will be only marginally better than Fiscal Year 2010. The past year we were able to avoid layoffs and service cuts largely due to our city employees taking deep cuts in pay. Fiscal Year 2011 will call for the same. The same factors that applied in Fiscal Year 2010 will apply in Fiscal Year 2011. Cuts to State Aid, and stagnant local revenues, increased healthcare costs continue to plague the financial health of this municipality. However, rather than look back, we have moved on and made the hard choices in changing our Health Insurance Plan that will prove to be beneficial in stabilizing health care costs. The City has not placed the burden on the taxpayer for the economic shortfall, as evidenced by having \$ 3,521,883 in excess levy capacity. Although this is good news for our taxpayers, it has become a hindrance in our ability to borrow temporarily. Situations such as the health insurance deficit in fiscal year 2010 called for the use of the Stabilization Fund. With such a dramatic change in our health insurance plan, it was the hope of the City to temporarily borrow for the deficit and reimburse the Stabilization funds that were used to offset the previous year's health insurance deficit. Unfortunately, the Department of Revenue felt differently and pointed us towards our unused levy capacity to offset the deficit. With the administration unwillingly to move in that direction, we are working within the operating budget to rejuvenate our Stabilization Fund to make it whole.

The City is also in the process of building and modifying a new High School for a projected cost of \$ 94,036,463. The City will receive a state reimbursement rate of 68.84 percent, which equates to \$ 64,734,701. The City has structured the borrowing for the High School so that the combination of existing debt retiring and the utilization of Stabilization Funds will have no impact on the taxpayer for the City's share of the cost of construction.

Among other economic factors benefiting the City is the sale of the Holy Family Hospital, which was owned by Caritas Christi, to Steward Health Care System, a newly formed affiliate of Cerberus Capital Management. As a result of the transaction, the Caritas system will no longer operate on a nonprofit, tax-free basis, and the hospital will begin paying all applicable state and local taxes. In Methuen, the sale means a hefty increase in property taxes. Holy Family Hospital's building and land is worth almost \$ 49 million. Based on the timing of the sale, the City will capture a payment in Lieu of Taxes in Fiscal Year 2011, along with increased permitting fees and add an additional \$ 1,069,218 in property taxes moving forward.

We still firmly believe the adoption of, and adherence to, a comprehensive strategy to regain structural balance with concurrent replenishment of reserves will be critical in enhancing Methuen's long term financial outlook.

The budget, tax levies, tax rates and values of the General Fund and Enterprise Fund for subsequent fiscal years have been formalized. The following tables reflect the budget amounts, at the time if tax rate setting each year.

General Fund Budget

| | FY 2010 | FY 2011 | Increase (Decrease) | % Change |
|-----------------|-------------------|-------------------|------------------------|--------------|
| City | \$ 55,784 (1) | \$ 59,117 (1) | \$ 3,333 | 5.97% |
| School | \$ 62,032 | \$ 63,303 | \$ 1,271 | 2.05% |
| County | \$ 1,366 | \$ 1,484 | \$ 118 | 8.64% |
| Enterprise Fund | \$ 9,254 (2) | \$ 9,072 (2) | \$ (182) | -1.97% |
| Total Budget | <u>\$ 128,436</u> | <u>\$ 132,976</u> | <u>\$ 4,540</u> | <u>3.53%</u> |

(1) Includes reserve for abatements and exemptions and cherry sheet offets.

(2) Excludes indirect costs.

Tax Levy

| | FY 2010 | FY 2011 | Increase (Decrease) | % Change |
|--------------------|------------------|------------------|------------------------|--------------|
| General Government | \$ 18,302 | \$ 16,964 | \$ (1,338) | -7.31% |
| Fixed Costs | \$ 17,226 | \$ 20,095 | \$ 2,869 | 16.66% |
| School | \$ 25,410 | \$ 24,686 | \$ (724) | -2.85% |
| Overlay | \$ 359 | \$ 309 | \$ (50) | -13.93% |
| Court Judgment | \$ - | \$ 134 | \$ 134 | 100.00% |
| Total Levy | <u>\$ 61,297</u> | <u>\$ 62,188</u> | <u>\$ 891</u> | <u>1.45%</u> |

(continued)

(continued)

| <u>Tax Rate</u> | <u>FY 2010</u> | <u>FY 2011</u> | <u>Increase (Decrease)</u> | <u>% Change</u> |
|-----------------|----------------|----------------|--------------------------------|-----------------|
| Residential | \$ 11.86 | \$ 12.69 | \$ 0.83 | 7.00% |
| Commercial | \$ 21.91 | \$ 22.91 | \$ 1.00 | 4.56% |

Valuation by Classification

| <u>Classification</u> | <u>FY 2010</u> | <u>FY 2011</u> | <u>Increase (Decrease)</u> | <u>% Change</u> |
|-----------------------|---------------------|---------------------|--------------------------------|-----------------|
| Residential | \$ 3,901,280 | \$ 3,692,062 | \$ (209,218) | -5.36% |
| Commercial | \$ 379,346 | \$ 370,636 | \$ (8,710) | -2.30% |
| Industrial | \$ 156,094 | \$ 150,992 | \$ (5,102) | -3.27% |
| Personal Property | \$ 150,471 | \$ 147,772 | \$ (2,699) | -1.79% |
| | <u>\$ 4,587,191</u> | <u>\$ 4,361,462</u> | <u>\$ (225,729)</u> | <u>-4.92%</u> |

Utility Fund Budget

| | <u>FY 2010</u> | <u>FY 2011</u> | <u>Increase (Decrease)</u> | <u>% Change</u> |
|-------------------------------|----------------|----------------|--------------------------------|-----------------|
| Water & Sewer Enterprise Fund | \$ 10,498 | \$ 10,338 | \$ (160) | -1.52% |

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City of Methuen's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

City Auditor
City of Methuen
41 Pleasant Street
Methuen, MA 01844

CITY OF METHUEN, MASSACHUSETTS

STATEMENT OF NET ASSETS

JUNE 30, 2010

| | <u>Governmental Activities</u> | <u>Business-Type Activities</u> | <u>Total</u> |
|---|--------------------------------|---------------------------------|----------------------|
| ASSETS | | | |
| Current: | | | |
| Cash and short-term investments | \$ 7,632,468 | \$ 3,693,855 | \$ 11,326,323 |
| Receivables, net of allowance for uncollectibles: | | | |
| Property taxes | 3,075,760 | - | 3,075,760 |
| Excises | 1,022,310 | - | 1,022,310 |
| User fees | - | 4,624,388 | 4,624,388 |
| Assessments | 239,384 | - | 239,384 |
| Departmental and other | 2,794,980 | - | 2,794,980 |
| Intergovernmental | 903,330 | 64,517 | 967,847 |
| Loans | 2,833,459 | - | 2,833,459 |
| Total current assets | 18,501,691 | 8,382,760 | 26,884,451 |
| Noncurrent: | | | |
| Property taxes | 290,909 | - | 290,909 |
| Deferred debt expense | 702,978 | - | 702,978 |
| Capital assets: | | | |
| Nondepreciable capital assets | 10,866,339 | 251,550 | 11,117,889 |
| Other capital assets, net of accumulated depreciation | 73,988,512 | 39,992,826 | 113,981,338 |
| Total noncurrent assets | 85,848,738 | 40,244,376 | 126,093,114 |
| TOTAL ASSETS | 104,350,429 | 48,627,136 | 152,977,565 |
| LIABILITIES | | | |
| Current: | | | |
| Accounts payable | 1,619,827 | 277,623 | 1,897,450 |
| Accrued liabilities | 1,843,623 | 342,368 | 2,185,991 |
| Unearned revenue | - | 497,134 | 497,134 |
| Notes payable | 1,210,000 | 638,836 | 1,848,836 |
| Other current liabilities | 2,206,690 | - | 2,206,690 |
| Current portion of long-term liabilities: | | | |
| Bonds and loans payable | 7,055,000 | 1,298,312 | 8,353,312 |
| Other liabilities | 2,015,064 | 35,200 | 2,050,264 |
| Total current liabilities | 15,950,204 | 3,089,473 | 19,039,677 |
| Noncurrent: | | | |
| Bonds and loans payable, net of current portion | 35,855,000 | 24,994,657 | 60,849,657 |
| Net OPEB obligation | 19,188,956 | 503,576 | 19,692,532 |
| Other liabilities, net of current portion | 2,636,056 | 300,898 | 2,936,954 |
| Total noncurrent liabilities | 57,680,012 | 25,799,131 | 83,479,143 |
| TOTAL LIABILITIES | 73,630,216 | 28,888,604 | 102,518,820 |
| NET ASSETS | | | |
| Invested in capital assets, net of related debt | 42,255,118 | 13,372,114 | 55,627,232 |
| Restricted externally or constitutionally for: | | | |
| Loan and grant programs | 459,589 | - | 459,589 |
| Permanent fund: | | | |
| Nonexpendable | 476,392 | - | 476,392 |
| Unrestricted | (12,470,886) | 6,366,418 | (6,104,468) |
| TOTAL NET ASSETS | \$ 30,720,213 | \$ 19,738,532 | \$ 50,458,745 |

CITY OF METHUEN, MASSACHUSETTS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2010

| | <u>Expenses</u> | Program Revenues | | |
|----------------------------------|-----------------------|-----------------------------|---|---|
| | | <u>Charges for Services</u> | <u>Operating Grants and Contributions</u> | <u>Capital Grants and Contributions</u> |
| Governmental Activities: | | | | |
| General government | \$ 13,589,259 | \$ 1,366,672 | \$ 68,799 | \$ - |
| Public safety | 21,100,997 | 3,484,704 | 319,562 | - |
| Education | 101,866,136 | 2,779,462 | 55,539,601 | - |
| Public works | 8,917,825 | 303,748 | 594,327 | 1,898,763 |
| Sanitation | 2,440,244 | - | - | - |
| Health and human services | 1,312,888 | 106,063 | 108,807 | - |
| Culture and recreation | 1,939,535 | 1,362,879 | 10,265 | - |
| Interest | 2,007,203 | - | - | - |
| Total Governmental Activities | 153,174,087 | 9,403,528 | 56,641,361 | 1,898,763 |
| Business-Type Activities: | | | | |
| Enterprise services | <u>8,521,552</u> | <u>10,703,206</u> | <u>16,554</u> | <u>-</u> |
| Total | <u>\$ 161,695,639</u> | <u>\$ 20,106,734</u> | <u>\$ 56,657,915</u> | <u>\$ 1,898,763</u> |

General Revenues and Transfers:

Property taxes
 Excise taxes
 Interest and penalties
 Grants and contributions not restricted
 to specific programs
 Investment income
 Other
 Transfers, net

Total general revenues and transfers

Change in Net Assets

Net Assets:

Beginning of year

End of year

See notes to financial statements.

Net (Expenses) Revenues and Changes in Net Assets

| <u>Governmental Activities</u> | <u>Business-Type Activities</u> | <u>Total</u> |
|--------------------------------|---------------------------------|--------------------------|
| \$ (12,153,788) | \$ - | \$ (12,153,788) |
| (17,296,731) | - | (17,296,731) |
| (43,547,073) | - | (43,547,073) |
| (6,120,987) | - | (6,120,987) |
| (2,440,244) | - | (2,440,244) |
| (1,098,018) | - | (1,098,018) |
| (566,391) | - | (566,391) |
| <u>(2,007,203)</u> | <u>-</u> | <u>(2,007,203)</u> |
| (85,230,435) | - | (85,230,435) |
| - | <u>2,198,208</u> | <u>2,198,208</u> |
| (85,230,435) | 2,198,208 | (83,032,227) |
| 61,118,256 | - | 61,118,256 |
| 4,352,271 | - | 4,352,271 |
| 374,721 | - | 374,721 |
| 12,188,948 | - | 12,188,948 |
| 58,988 | 9,583 | 68,571 |
| 1,337,644 | - | 1,337,644 |
| <u>1,244,613</u> | <u>(1,244,613)</u> | <u>-</u> |
| <u>80,675,441</u> | <u>(1,235,030)</u> | <u>79,440,411</u> |
| (4,554,994) | 963,178 | (3,591,816) |
| <u>35,275,207</u> | <u>18,775,354</u> | <u>54,050,561</u> |
| \$ <u>30,720,213</u> | \$ <u>19,738,532</u> | \$ <u>50,458,745</u> |

CITY OF METHUEN, MASSACHUSETTS

GOVERNMENTAL FUNDS

BALANCE SHEET

JUNE 30, 2010

| ASSETS | <u>General</u> | Nonmajor Governmental Funds | Total Governmental Funds |
|---------------------------------|----------------------|-----------------------------------|--------------------------------|
| Cash and short-term investments | \$ 3,198,747 | \$ 4,433,721 | \$ 7,632,468 |
| Receivables: | | | |
| Property taxes | 3,652,637 | - | 3,652,637 |
| Excises | 1,267,335 | - | 1,267,335 |
| Assessments | 239,384 | - | 239,384 |
| Departmental and other | 1,689,415 | 584,089 | 2,273,504 |
| Intergovernmental | - | 903,330 | 903,330 |
| Loans | - | 2,833,459 | 2,833,459 |
| Due from other funds | <u>1,524,441</u> | <u>1,440,000</u> | <u>2,964,441</u> |
| TOTAL ASSETS | <u>\$ 11,571,959</u> | <u>\$ 10,194,599</u> | <u>\$ 21,766,558</u> |

LIABILITIES AND FUND BALANCES

| | | | |
|---|----------------------|----------------------|----------------------|
| Liabilities: | | | |
| Warrants and accounts payable | \$ 1,232,234 | \$ 387,125 | \$ 1,619,359 |
| Accrued liabilities | 1,097,976 | 268,165 | 1,366,141 |
| Deferred revenues | 5,725,602 | 3,089,117 | 8,814,719 |
| Notes payable | - | 1,210,000 | 1,210,000 |
| Other liabilities | <u>1,083,555</u> | <u>7,326</u> | <u>1,090,881</u> |
| TOTAL LIABILITIES | 9,139,367 | 4,961,733 | 14,101,100 |
| Fund Balances: | | | |
| Reserved for: | | | |
| Encumbrances | 805,750 | - | 805,750 |
| Other purposes | 520,997 | 1,440,000 | 1,960,997 |
| Perpetual permanent fund | - | 476,392 | 476,392 |
| Unreserved - undesignated, reported in: | | | |
| General fund | 1,105,845 | - | 1,105,845 |
| Special revenue funds | - | 3,937,229 | 3,937,229 |
| Capital project funds | - | (620,755) | (620,755) |
| TOTAL FUND BALANCES | <u>2,432,592</u> | <u>5,232,866</u> | <u>7,665,458</u> |
| TOTAL LIABILITIES AND FUND BALANCES | <u>\$ 11,571,959</u> | <u>\$ 10,194,599</u> | <u>\$ 21,766,558</u> |

CITY OF METHUEN, MASSACHUSETTS

RECONCILIATION OF TOTAL GOVERNMENTAL FUND
BALANCES TO NET ASSETS OF GOVERNMENTAL
ACTIVITIES IN THE STATEMENT OF NET ASSETS

JUNE 30, 2010

| | |
|--|----------------------|
| Total governmental fund balances | \$ 7,665,458 |
| • Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. | 84,854,851 |
| • Deferred debt expense for refunding is net of amortization on the statement of net assets, whereas all debt expense is reported when paid in the governmental funds. | 702,978 |
| • Revenues are reported on the accrual basis of accounting and are not deferred until collection. | 8,059,935 |
| • Internal service funds are used by management to account for health insurance and workers' compensation activities. The assets and liabilities of the internal service funds are included in the governmental activities in the Statement of Net Assets. | (3,335,453) |
| • In the statement of activities, interest is accrued on outstanding long-term debt, whereas in governmental funds interest is not reported until due. | (477,480) |
| • Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds. | |
| Bonds payable | (42,910,000) |
| Capital lease payable | (371,957) |
| Net OPEB obligation | (19,188,956) |
| Landfill liability | (720,000) |
| Compensated absences liability | <u>(3,559,163)</u> |
| Net assets of governmental activities | <u>\$ 30,720,213</u> |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS

GOVERNMENTAL FUNDS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

FOR THE YEAR ENDED JUNE 30, 2010

| | General | Nonmajor Governmental Funds | Total Governmental Funds |
|--|---------------------|-----------------------------------|--------------------------------|
| Revenues: | | | |
| Property taxes | \$ 60,968,684 | \$ - | \$ 60,968,684 |
| Excise taxes | 4,243,585 | - | 4,243,585 |
| Departmental | 1,995,240 | - | 1,995,240 |
| Licenses and permits | 1,071,028 | - | 1,071,028 |
| Intergovernmental | 56,968,373 | 13,472,297 | 70,440,670 |
| Charges for services | 36,692 | 5,783,111 | 5,819,803 |
| Interest and penalties | 374,721 | - | 374,721 |
| Investment income | 20,412 | 38,576 | 58,988 |
| Fines and forfeitures | 220,783 | - | 220,783 |
| Contributions | - | 96,388 | 96,388 |
| Other revenue | 1,098,056 | 239,588 | 1,337,644 |
| Total Revenues | <u>126,997,574</u> | <u>19,629,960</u> | <u>146,627,534</u> |
| Expenditures: | | | |
| Current: | | | |
| General government | 21,107,057 | 234,356 | 21,341,413 |
| Public safety | 15,273,527 | 2,260,184 | 17,533,711 |
| Education | 71,393,299 | 14,030,247 | 85,423,546 |
| Public works | 5,886,098 | 2,211,639 | 8,097,737 |
| Sanitation | 2,434,361 | 5,883 | 2,440,244 |
| Health and human services | 980,737 | 191,362 | 1,172,099 |
| Culture and recreation | 1,027,988 | 910,732 | 1,938,720 |
| Debt service: | | | |
| Principal | 6,340,000 | - | 6,340,000 |
| Interest | 2,039,494 | - | 2,039,494 |
| Total Expenditures | <u>126,482,561</u> | <u>19,844,403</u> | <u>146,326,964</u> |
| Excess (deficiency) of revenues over expenditures | 515,013 | (214,443) | 300,570 |
| Other Financing Sources (Uses): | | | |
| Issuance of notes | 600,000 | - | 600,000 |
| Transfers in | 1,510,444 | 1,254,169 | 2,764,613 |
| Transfers out | <u>(1,589,251)</u> | - | <u>(1,589,251)</u> |
| Total Other Financing Sources (Uses) | <u>521,193</u> | <u>1,254,169</u> | <u>1,775,362</u> |
| Net change in fund balances | 1,036,206 | 1,039,726 | 2,075,932 |
| Fund Balances, at Beginning of Year | <u>1,396,386</u> | <u>4,193,141</u> | <u>5,589,527</u> |
| Fund Balances, at End of Year | <u>\$ 2,432,592</u> | <u>\$ 5,232,867</u> | <u>\$ 7,665,459</u> |

CITY OF METHUEN, MASSACHUSETTS

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

FOR THE YEAR ENDED JUNE 30, 2010

| NET CHANGES IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS | \$ 2,075,932 |
|--|-----------------------|
| • 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: | |
| Capital outlay purchases, net of disposals | 3,132,375 |
| Depreciation | (3,440,258) |
| • Revenues in the Statement of Activities that do not provide current financial resources are fully deferred in the Statement of Revenues, Expenditures and Changes in Fund Balances. Therefore, the recognition of revenue for various types of accounts receivable (i.e., real estate and personal property, motor vehicle excise, etc.) differ between the two statements. This amount represents the net change in deferred revenue. | 746,948 |
| • The issuance of long-term debt (e.g., bonds and leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the financial resources of governmental funds. Neither transaction, however, has any effect on net assets: | |
| Repayments of debt | 6,340,000 |
| Issuance of notes | (600,000) |
| Deferred debt amortization | (140,595) |
| Payments of capital leases | 288,477 |
| • In the statement of activities, interest is accrued on outstanding long-term debt, whereas in governmental funds interest is not reported until due. | 32,292 |
| • Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore, are not reported as expenditures in the governmental funds. | |
| Compensated absences | (169,484) |
| Landfill | 40,000 |
| Net OPEB obligation | (9,594,478) |
| • Internal service funds are used by management to account for health insurance and workers' compensation activities. The net activity of internal service funds is reported with Governmental Activities. | <u>(3,266,203)</u> |
| CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES | \$ (4,554,994) |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS

GENERAL FUND

STATEMENT OF REVENUES AND OTHER SOURCES, AND EXPENDITURES
AND OTHER USES - BUDGET AND ACTUAL

FOR THE YEAR ENDED JUNE 30, 2010

| | Budgeted Amounts | | | Variance with Final Budget Positive (Negative) |
|--|--------------------|--------------------|--------------------|---|
| | Original Budget | Final Budget | Actual Amounts | |
| Revenues and Other Sources: | | | | |
| Property tax | \$ 60,834,329 | \$ 60,834,329 | \$ 60,834,329 | \$ - |
| Local revenue | 9,115,000 | 9,115,000 | 9,155,516 | 40,516 |
| Cherry sheet and misc | 46,925,633 | 46,925,633 | 47,034,608 | 108,975 |
| Transfers in | 1,509,641 | 1,526,444 | 1,526,444 | - |
| Other financing sources | <u>251,784</u> | <u>1,883,030</u> | <u>1,987,179</u> | <u>104,149</u> |
| Total Revenues and Other Sources | 118,636,387 | 120,284,436 | 120,538,076 | 253,640 |
| Expenditures and Other Uses: | | | | |
| Current: | | | | |
| General government | 21,898,908 | 22,495,276 | 21,839,582 | 655,694 |
| Intergovernmental | 1,366,219 | 1,362,794 | 1,362,794 | - |
| Public safety | 15,284,720 | 15,227,476 | 15,227,476 | - |
| Education | 62,032,126 | 61,345,946 | 61,345,946 | - |
| Public works | 5,066,361 | 5,458,174 | 5,458,154 | 20 |
| Sanitation | 2,490,974 | 2,446,599 | 2,446,599 | - |
| Library | 1,412,463 | 1,412,463 | 1,412,463 | - |
| Health and human services | 999,279 | 888,222 | 888,222 | - |
| Debt service | 7,952,869 | 8,015,018 | 8,015,018 | - |
| Transfers out | <u>132,468</u> | <u>1,632,468</u> | <u>1,632,468</u> | <u>-</u> |
| Total Expenditures and Other Uses | <u>118,636,387</u> | <u>120,284,436</u> | <u>119,628,722</u> | <u>655,714</u> |
| Excess of revenues and other sources over expenditures and other uses | \$ - | \$ - | \$ 909,354 | \$ 909,354 |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS

PROPRIETARY FUNDS

STATEMENT OF NET ASSETS

JUNE 30, 2010

| | <u>Business-Type Activities</u> | <u>Governmental Activities</u> |
|--|-------------------------------------|--------------------------------------|
| | <u>Enterprise Fund</u> | <u>Internal Service Fund</u> |
| <u>ASSETS</u> | | |
| Current: | | |
| Cash and short-term investments | \$ 3,693,855 | \$ - |
| User fees receivable | 4,624,388 | - |
| Intergovernmental receivable | 64,517 | - |
| Other receivables | <u>-</u> | <u>745,266</u> |
| Total current assets | 8,382,760 | 745,266 |
| Noncurrent: | | |
| Capital assets: | | |
| Nondepreciable capital assets | 251,550 | - |
| Other capital assets, net of accumulated depreciation | <u>39,992,826</u> | <u>-</u> |
| Total noncurrent assets | <u>40,244,376</u> | <u>-</u> |
| TOTAL ASSETS | 48,627,136 | 745,266 |
| <u>LIABILITIES</u> | | |
| Current: | | |
| Accounts payable | 277,623 | 469 |
| Accrued liabilities | 342,368 | - |
| Unearned revenue | 497,134 | - |
| Notes payable | 638,836 | - |
| Due to other funds | <u>-</u> | <u>2,964,441</u> |
| Other current liabilities | <u>-</u> | <u>1,115,809</u> |
| Current portion of long-term liabilities: | | |
| Bonds and loans payable | 1,298,312 | - |
| Other liabilities | <u>35,200</u> | <u>-</u> |
| Total current liabilities | 3,089,473 | 4,080,719 |
| Noncurrent: | | |
| Bonds and loans payable, net of current portion | 24,994,657 | - |
| Net OPEB obligation | 503,576 | - |
| Other liabilities, net of current portion | <u>300,898</u> | <u>-</u> |
| Total noncurrent liabilities | <u>25,799,131</u> | <u>-</u> |
| TOTAL LIABILITIES | 28,888,604 | 4,080,719 |
| <u>NET ASSETS</u> | | |
| Invested in capital assets, net of related debt | 13,372,114 | - |
| Unrestricted (See Note 19) | <u>6,366,418</u> | <u>(3,335,453)</u> |
| TOTAL NET ASSETS | \$ 19,738,532 | \$ (3,335,453) |

CITY OF METHUEN, MASSACHUSETTS

PROPRIETARY FUNDS

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

FOR THE YEAR ENDED JUNE 30, 2010

| | <u>Business-Type Activities</u> | <u>Governmental Activities</u> |
|---|-------------------------------------|--------------------------------------|
| | <u>Enterprise Fund</u> | <u>Internal Service Fund</u> |
| Operating Revenues: | | |
| Charges for services | \$ 10,499,241 | \$ - |
| Contributions | - | 15,437,524 |
| Permits and fees | <u>203,965</u> | <u>-</u> |
| Total Operating Revenues | 10,703,206 | 15,437,524 |
| Operating Expenses: | | |
| Personal services | 2,323,867 | - |
| Materials | 1,870,228 | - |
| Depreciation | 807,249 | - |
| Sanitary district assessment | 2,790,833 | - |
| Employee benefits | - | 18,772,978 |
| Other expenses | <u>123,312</u> | <u>-</u> |
| Total Operating Expenses | <u>7,915,489</u> | <u>18,772,978</u> |
| Operating Income | 2,787,717 | (3,335,454) |
| Nonoperating Revenues (Expenses): | | |
| Intergovernmental revenue | 16,554 | - |
| Investment income | 9,583 | - |
| Interest expense | <u>(606,063)</u> | <u>-</u> |
| Total Nonoperating Revenues (Expenses), Net | <u>(579,926)</u> | <u>-</u> |
| Income (Loss) Before Transfers | 2,207,791 | (3,335,454) |
| Transfers in | - | 69,251 |
| Transfers out | <u>(1,244,613)</u> | <u>-</u> |
| Change in Net Assets | 963,178 | (3,266,203) |
| Net Assets at Beginning of Year | <u>18,775,354</u> | <u>(69,250)</u> |
| Net Assets at End of Year | <u>\$ 19,738,532</u> | <u>\$ (3,335,453)</u> |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS

PROPRIETARY FUNDS

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2010

| | <u>Business-Type Activities</u> | <u>Governmental Activities</u> |
|--|---------------------------------|--------------------------------|
| | <u>Enterprise Fund</u> | <u>Internal Service Fund</u> |
| <u>Cash Flows From Operating Activities:</u> | | |
| Receipts from customers and users | \$ 10,390,311 | \$ - |
| Employer contributions and stop loss reimbursements | - | 9,393,366 |
| Employee contributions | - | 5,394,120 |
| Payments of employee salaries, benefits, and related expenses | (2,051,582) | (18,449,782) |
| Payments to vendors | (1,860,338) | - |
| Payments to other governments | <u>(2,790,833)</u> | <u>-</u> |
| Net Cash Provided By Operating Activities | 3,687,558 | (3,662,296) |
| <u>Cash Flows From Noncapital Financing Activities:</u> | | |
| Transfers from other funds | - | 69,251 |
| Advances from general fund | - | 2,964,441 |
| Transfers to other funds | <u>(1,244,613)</u> | <u>-</u> |
| Net Cash (Used For) Noncapital Financing Activities | (1,244,613) | 3,033,692 |
| <u>Cash Flows From Capital and Related Financing Activities:</u> | | |
| Acquisition and construction of capital assets | (534,084) | - |
| Proceeds from bonds and notes | 1,096,906 | - |
| Principal payments on bonds, notes, and capital leases | (1,265,602) | - |
| Interest expense | (624,265) | - |
| Intergovernmental subsidy | <u>16,554</u> | <u>-</u> |
| Net Cash (Used For) Capital and Related Financing Activities | (1,310,491) | - |
| <u>Cash Flows From Investing Activities:</u> | | |
| Investment income | <u>9,585</u> | <u>-</u> |
| Net Cash Provided By Investing Activities | <u>9,585</u> | <u>-</u> |
| Net Change in Cash and Short-Term Investments | 1,142,039 | (628,604) |
| Cash and Short-Term Investments, Beginning of Year | <u>2,551,816</u> | <u>628,604</u> |
| Cash and Short-Term Investments, End of Year | <u>\$ 3,693,855</u> | <u>\$ -</u> |
| <u>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</u> | | |
| Operating income | \$ 2,787,717 | \$ (3,335,454) |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation | 807,249 | - |
| Changes in assets and liabilities: | | |
| User fees | (440,241) | - |
| Other receivables | - | (650,038) |
| Accounts payable | 133,198 | (1,031) |
| Accrued liabilities | 11,727 | - |
| Unearned revenue | 127,350 | - |
| Other liabilities | - | 324,227 |
| Compensated absences | 8,770 | - |
| OPEB liability | <u>251,788</u> | <u>-</u> |
| Net Cash Provided By Operating Activities | <u>\$ 3,687,558</u> | <u>\$ (3,662,296)</u> |

CITY OF METHUEN, MASSACHUSETTS

FIDUCIARY FUNDS

STATEMENT OF FIDUCIARY NET ASSETS

JUNE 30, 2010

| | Pension Trust Fund (As of <u>December 31, 2009</u>) | Private Purpose Trust Fund | Agency Fund |
|---|---|-------------------------------------|----------------|
| <u>ASSETS</u> | | | |
| Non-pooled cash and short-term investments | \$ 1,488,271 | \$ 427,847 | \$ 138,130 |
| Investments, at fair value: | | | |
| Pooled alternative investments | 1,976,274 | - | - |
| Pooled real estate funds | 3,810,544 | - | - |
| PRIT Fund | 61,624,285 | - | - |
| Receivables | <u>613,397</u> | <u>-</u> | <u>-</u> |
| | | | |
| Total Assets | 69,512,771 | 427,847 | 138,130 |
| <u>LIABILITIES AND NET ASSETS</u> | | | |
| Other liabilities | <u>846</u> | <u>-</u> | <u>138,130</u> |
| | | | |
| Total Liabilities | <u>846</u> | <u>-</u> | <u>138,130</u> |
| <u>NET ASSETS</u> | | | |
| Total net assets held in trust for pension benefits and other purposes | <u>\$ 69,511,925</u> | <u>\$ 427,847</u> | <u>\$ -</u> |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS
 FIDUCIARY FUNDS
 STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
 FOR THE YEAR ENDED JUNE 30, 2010

| | Pension Trust Fund (For the Year Ended <u>December 31, 2009</u>) | Private Purpose Trust Fund |
|--|--|----------------------------------|
| Additions: | | |
| Contributions: | | |
| Employers | \$ 6,600,000 | \$ - |
| Other systems and Commonwealth of Massachusetts | 367,947 | - |
| Plan members | 2,952,562 | - |
| Other | 43,403 | - |
| Total contributions | <u>9,963,912</u> | <u>-</u> |
| Investment Income: | | |
| Change in fair value of investments | 6,645,945 | 723 |
| Less: management fees | <u>(378,489)</u> | <u>-</u> |
| Net investment income (loss) | <u>6,267,456</u> | <u>723</u> |
| Total additions | <u>16,231,368</u> | <u>723</u> |
| Deductions: | | |
| Benefit payments to plan members and beneficiaries | 8,998,787 | - |
| Refunds to plan members | 186,292 | - |
| Transfers to other systems | 38,659 | - |
| Administrative expenses | 204,161 | - |
| Other | <u>-</u> | <u>35,000</u> |
| Total deductions | <u>9,427,899</u> | <u>35,000</u> |
| Net increase (decrease) | 6,803,469 | (34,277) |
| Net assets: | | |
| Beginning of year | <u>62,708,456</u> | <u>462,124</u> |
| End of year | <u>\$ 69,511,925</u> | <u>\$ 427,847</u> |

See notes to financial statements.

CITY OF METHUEN, MASSACHUSETTS

Notes to Financial Statements

1. Summary of Significant Accounting Policies

The accounting policies of the City of Methuen (the City) conform to generally accepted accounting principles (GAAP) as applicable to governmental units. The following is a summary of the more significant policies:

A. Reporting Entity

The government is a municipal corporation governed by an elected City Council. As required by generally accepted accounting principles, these financial statements present the government and applicable component units for which the government is considered to be financially accountable.

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

In the Fiduciary Funds: The Methuen Contributory Retirement System which was established to provide retirement benefits primarily to employees and their beneficiaries. The System is presented using the accrual basis of accounting and is reported as a pension trust fund in the fiduciary fund financial statements. Additional financial information of the System can be obtained by contacting the System located at 41 Pleasant Street, Methuen, MA 01844.

B. Government-Wide and Fund Financial Statements

Government-Wide Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues.

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

Fund Financial Statements

Separate financial statements are provided for governmental funds, proprietary funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

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

Government-Wide Financial Statements

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as is the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

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 and excises.

Fund Financial Statements

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

related to compensated absences and claims and judgments, are recorded only when payment is due.

The government reports the following major governmental fund:

- The *general fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

Proprietary funds distinguish operating revenues and expenses from non-operating 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 enterprise fund are charges to customers for sales and services. 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.

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

The *enterprise fund* accounts for the operating activities of the City's water and sewer utilities and capital improvement services.

The self-insured employee health program is reported as an *internal service fund* in the accompanying financial statements.

The *pension trust fund* accounts for the activities of the Employees Contributory Retirement System, which accumulates resources for pension benefit payments to qualified employees.

The *private-purpose trust fund* is used to account for trust arrangements, under which principal and investment income exclusively benefit individuals, private organizations, or other governments.

The *agency fund* is used to account for student activity funds.

D. Cash and Short-Term Investments

Cash balances from all funds, except those required to be segregated by law, are combined to form a consolidation of cash. Cash balances are invested to

the extent available, and interest earnings are recognized in the General Fund. Certain special revenue, proprietary, permanent, and fiduciary funds segregate cash, and investment earnings become a part of those funds.

Deposits with financial institutions consist primarily of demand deposits, certificates of deposits, and savings accounts. A cash and investment pool is maintained that is available for use by all funds. Each fund's portion of this pool is reflected on the combined financial statements under the caption "cash and short-term investments". The interest earnings attributable to each fund type are included under investment income.

For purpose of the statement of cash flows, the proprietary funds consider investments with original maturities of three months or less to be short-term investments.

State and local statutes place certain limitations on the nature of deposits and investments available. Deposits in any financial institution may not exceed certain levels within the financial institution. Non-fiduciary fund investments can be made in securities issued by or unconditionally guaranteed by the U.S. Government or agencies that have a maturity of one year or less from the date of purchase and repurchase agreements guaranteed by such securities with maturity dates of no more than 90 days from the date of purchase.

Trust Funds may be combined and invested in any instruments allowed by Legal List issued by the Banking Commissioner, except those required to be segregated by trust documents. Each trust fund is accounted for separately.

E. Investments

The City did not have long-term investments as of June 30, 2010. The System's investments are carried at market value.

F. Property Tax Limitations

The City has limited the amount of revenue that can be derived from property taxes. The prior fiscal year's tax levy limit is used as a base and cannot increase by more than 2.5 percent (excluding new growth), unless an override or debt exemption is voted. The actual fiscal year 2010 tax levy reflected an excess capacity of approximately \$ 2,041,030.

G. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets, (for enterprise funds only) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial individual cost of more than \$ 5,000 and an estimated useful life in excess of

five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant and equipment is depreciated using the straight-line method over the following estimated useful lives:

| <u>Assets</u> | <u>Years</u> |
|---------------------------------|--------------|
| Land improvements | 20 |
| Construction | 25 - 50 |
| Infrastructure | 10 - 30 |
| Equipment | 5 - 20 |
| Machinery and licensed vehicles | 8 |

H. Compensated Absences

The government's policy is to permit employees to accumulate earned but unused vacation and sick pay benefits. Full-time, permanent employees are granted vacation benefits in varying amounts depending on contracts with the City. Sick leave accrues to full-time, permanent employees to specified maximums. Generally, after one year of service, employees are entitled to a percentage of their sick leave ranging between 30% and 50% depending on their contract with the City, and all of their accrued vacation upon termination. All vested sick and vacation pay is accrued when incurred in the government-wide, proprietary and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

I. 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.

J. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

K. Use of Estimates

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

In prior years, IBNR (see note 26) was estimated by taking a sum of claims paid in July, one half of those paid in August, and one quarter of those paid in September of the subsequent fiscal year. For the fiscal year ended June 30, 2009, Tufts Health Plan calculated the IBNR on the City's behalf, using actual utilization data to assign costs more accurately to the fiscal year in which they were truly incurred. As a result, the City believes that the current estimate is more accurate and reasonable.

2. Stewardship, Compliance, and Accountability

A. Budgetary Information

At a City Council meeting in May, the Mayor presents an operating and capital budget for the proposed expenditures of the fiscal year commencing the following July 1. The budget, as enacted by the City Council, also establishes the legal level of control and specifies that certain appropriations are to be funded by particular revenues. The original budget is amended during the fiscal year at City Council meetings as required by changing conditions. In cases of extraordinary or unforeseen expenses, the City Council is empowered to transfer funds from the Reserve Fund to a departmental appropriation. "Extraordinary" includes expenses which are not in the usual line, or are great or exceptional. "Unforeseen" includes expenses which are not foreseen as of the time of the annual meeting when appropriations are voted.

Departments are limited to the major line items as voted by the City Council. Certain items may exceed the line item budget as approved if it is for an emergency and for the safety of the general public. These items are limited

by the Massachusetts General Laws, and must be raised in the next year's tax rate.

Annually, prior to year-end, the City Council authorizes the Mayor and City Accountant to amend the budget by making various inter and intradepartmental transfers and using available sources to avoid individual departmental over-expenditures.

At year-end, appropriation balances lapse, except for certain unexpended capital items and encumbrances, which will be honored during the subsequent year.

Formal budgetary integration is employed as a management control device during the year for the General Fund and Enterprise Funds.

Effective budgetary control is achieved for all other funds through provisions of the Massachusetts General Laws.

B. Budgetary Basis

The General Fund final appropriation appearing on the "Budget and Actual" page of the fund financial statements represents the final amended budget after all reserve fund transfers and supplemental appropriations.

C. Budget/GAAP Reconciliation

The budgetary data for the general and proprietary funds is based upon accounting principles that differ from generally accepted accounting principles (GAAP). Therefore, in addition to the GAAP basis financial statements, the results of operations of the general fund are presented in accordance with budgetary accounting principles to provide a meaningful comparison with budgetary data.

The following is a summary of adjustments made to the actual revenues and other sources, and expenditures and other uses, to conform to the budgetary basis of accounting.

| <u>General Fund</u> | <u>Revenues and Other Financing Sources</u> | <u>Expenditures and Other Financing Uses</u> |
|--|---|--|
| Revenues/Expenditures (GAAP basis) | \$ 126,997,574 | \$ 126,482,561 |
| Other financing sources/uses (GAAP basis) | 2,110,444 | 1,589,251 |
| Subtotal (GAAP Basis) | 129,108,018 | 128,071,812 |

(continued)

(continued)

| <u>General Fund</u> | <u>Revenues and Other Financing Sources</u> | <u>Expenditures and Other Financing Uses</u> |
|---|---|--|
| To adjust property tax revenue to the budgetary basis | 113,053 | - |
| Reverse beginning of year appropriation carryforwards from expenditures | - | (613,062) |
| To book current year appropriation carryforwards | - | 805,750 |
| To record raising of prior years' snow and ice deficit | - | 63,217 |
| To record use of overlay | 16,000 | - |
| To reverse GASB 24 MTRS | (8,889,711) | (8,889,711) |
| To gross up education allocation of employee benefits | <u>190,716</u> | <u>190,716</u> |
| Budgetary basis | <u>\$ 120,538,076</u> | <u>\$ 119,628,722</u> |

D. Deficit Fund Equity

The following funds or projects within the funds had deficits as of June 30, 2010:

Nonmajor Governmental Funds:

| | |
|--------------------------------------|------------|
| Law Enforcement Grants | \$ 3,407 |
| Home Program | \$ 4,760 |
| Police Outside Detail | \$ 220,791 |
| Fire Staffing Stimulus Grant | \$ 109,345 |
| MA Cultural Council LLC | \$ 1,878 |
| Safe Schools and Communities | \$ 3,033 |
| Police Weed and Seed | \$ 24,957 |
| IDEA Stimulus Grant | \$ 13,795 |
| Perkins Grant | \$ 17,041 |
| Tech Enhancement | \$ 3,122 |
| CDBG-NSP FY08 Grant | \$ 5,901 |
| Appleyards Remediation/Redevelopment | \$ 3,369 |
| Recreation high school track | \$ 210,000 |
| Methuen High School Revitalization | \$ 739,257 |

Internal Service Fund:

| | |
|--------------------------------|--------------|
| Health Insurance (See Note 19) | \$ 3,335,453 |
|--------------------------------|--------------|

The deficits in these funds will be eliminated through future departmental revenues, bond proceeds, and transfers from other funds.

3. Cash and Short-Term Investments

Custodial Credit Risk. Custodial credit risk is the risk that in the event of a bank failure, the City's and Contributory Retirement System's (the System) deposits may not be returned. Massachusetts General Law Chapter 44, Section 55, limits deposits "in a bank or trust company or banking company to an amount not exceeding sixty percent of the capital and surplus of such bank or trust company or banking company, unless satisfactory security is given to it by such bank or trust company or banking company for such excess." Massachusetts General Law Chapter 32, Section 23, limits the System's deposits "in a bank or trust company to an amount not exceeding ten percent of the capital and surplus of such bank or trust company."

As of June 30, 2010, \$ 10,528,154 of the City's bank balances of \$ 17,127,251 was exposed to custodial credit risk as uninsured, and collateral held by pledging bank's trust department not in the System's name. The exposed balance was invested in the Massachusetts Municipal Depository Trust (MMDT), which is not considered an uncollateralized product under Government Accounting Standards Board Regulation. Per the City's policy, the City may invest in MMDT, U.S. Treasury and Agencies up to one year maturity, bank accounts and Certificates of Deposits, which are fully insured by FDIC, DIF, or collateralized through a third party agreement, and certain mutual funds, under Chapter 44, Sec. 55 of MGL, as amended by Chapter 314 of the Acts of 1996. Unsecured deposits are limited to no more than 5% of an institution's assets and no more than 10% of the City's cash. To maintain adequate cash flow, the City's balances as of June 30, 2010 were deposited in MMDT and bank accounts (checking, savings, and money market accounts).

As of December 31, 2009, \$ 1,559,668 of the System's bank balances of \$ 1,809,693 was exposed to custodial credit risk as uninsured, and collateral held by pledging bank's trust department not in the System's name. Of the System's total exposed balance, \$ 1,388,318 was invested in MMDT. The System does not have a deposit policy for custodial credit risk.

4. Investments

A. Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment.

Massachusetts General Law, Chapter 32, Section 23, limits the investment of the Retirement System funds, to the extent not required for current disbursements, in the PRIT Fund or in securities, other than mortgages or collateral loans, which are legal for the investment of funds in savings banks under the laws of the Commonwealth, provided that no more than the established percentage of assets, is invested in any one security.

In accordance with Chapter 32 Section 22 of the Massachusetts General Laws, the System has transferred its investments to the Commonwealth's PRIT fund because its funding ratio and rate of return in prior years has not met the standards established by PERAC.

At December 31, 2009, the System's investments consisted of the following:

| <u>Investment Type</u> | <u>Fair Value</u> |
|--------------------------|----------------------|
| Pooled Alternative Funds | \$ 1,976,274 |
| Pooled Real Estate Funds | 3,810,544 |
| State Investment Pool* | <u>61,624,285</u> |
| Total investments | <u>\$ 67,411,103</u> |

These investments are not rated.

**Fair value is the same as the value of the pool share. The Pension Reserves Investment Trust was created under Massachusetts General Law, Chapter 32, Section 22, in December 1983. The Pension Reserves Investment Trust is operated under contract with a private investment advisor, approved by the Pension Reserves Investment Management Board. The Pension Reserves Investment Management Board shall choose an investment advisor by requesting proposals from advisors and reviewing such proposals based on criteria adopted under Massachusetts General Law, Chapter 30B.*

B. Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The System does not have a policy for custodial credit risk.

The System's investment in Pooled funds of \$ 67,411,103 were exposed to custodial credit risk because the related securities are uninsured, unregistered and held by the system's brokerage firm, which is also the Counterparty to these securities. The System manages this risk with SIPC, Excess SIPC and because the assets are held in separately identifiable trust accounts. Of the System's total exposure, \$ 61,624,285 is invested in the State Investment Pool.

C. Concentration of Credit Risk

The City's policy prohibits concentration in any one issuer. The City did not have any long-term investments at June 30, 2010.

Massachusetts General Law Chapter 32, Section 23 limits the amount the System may invest in any one issuer or security type, with the exception of the PRIT Fund.

The System does not have an investment in one issuer greater than 5% of total investments, with the exception of the PRIT Fund.

D. Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The City's current policy does not allow maturities of over one year. The current objective of the City is to have highly liquid investments (see note 3) to sustain adequate cash flow needs of the City. The System does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

E. Foreign Currency Risk

Foreign currency risk is the risk that changes in foreign exchange rates will adversely affect the fair value of an investment. The City does not have foreign investments. The System does not have a foreign currency risk policy.

5. Taxes Receivable

Real estate and personal property taxes are levied and based on values assessed on January 1st of every year. Assessed values are established by the Board of Assessor's for 100% of the estimated fair market value. Taxes are due on a quarterly basis and are subject to penalties and interest if they are not paid by the respective due date. Real estate and personal property taxes levied are recorded as receivables in the fiscal year they relate to.

Fourteen days after the due date for the final tax bill for real estate taxes, a demand notice may be sent to the delinquent taxpayer. Fourteen days after the demand notice has been sent, the tax collector may proceed to file a lien against the delinquent taxpayers' property. The City has an ultimate right to foreclose on property for unpaid taxes. Personal property taxes cannot be secured through the lien process.

Taxes receivable at June 30, 2010 consist of the following (in thousands):

| | | | |
|-------------------|------------|-----------------|--|
| Real Estate | | | |
| 2010 | | \$ 1,864 | |
| Personal Property | | | |
| 2010 | 28 | | |
| 2009 | 18 | | |
| 2008 | 13 | | |
| 2007 | 8 | | |
| Prior | <u>267</u> | | |
| | | 334 | |
| Tax Liens | | <u>1,455</u> | |
| Total | | \$ <u>3,653</u> | |

6. Allowance for Doubtful Accounts

The receivables reported in the accompanying entity-wide financial statements reflect the following estimated allowances for doubtful accounts (in thousands):

| | |
|----------------|--------|
| Property taxes | \$ 286 |
| Excises | 245 |

7. User Fees Receivable

User fees receivable in the enterprise fund includes amounts due from customers for water and sewer usage. Water and sewer delinquent receivables are liened in a similar manner as property taxes, described in Note 5.

8. Departmental and Other Receivables

The City's departmental and other receivables at June 30, 2010 consist of the following:

| | Fire | Police | Veterans | Other | Total |
|--|-------------------|-------------------|-------------------|---------------------|---------------------|
| | Ambulance | Outside Detail | Benefits | | |
| Gross | \$ 994,121 | \$ 255,658 | \$ 304,309 | \$ 1,464,682 | \$ 3,018,770 |
| Less: Allowance for doubtful accounts | <u>(198,224)</u> | <u>(25,566)</u> | <u>-</u> | <u>-</u> | <u>(223,790)</u> |
| Total | <u>\$ 795,897</u> | <u>\$ 230,092</u> | <u>\$ 304,309</u> | <u>\$ 1,464,682</u> | <u>\$ 2,794,980</u> |

9. Intergovernmental Receivables

This balance represents reimbursements requested from Federal and State agencies for expenditures incurred in fiscal 2010 and the amount to be drawn down from Massachusetts Water Pollution Abatement Trust for the improvement of the water distribution system, which is included in the City's long-term debt.

10. Loans Receivable

Loans receivable represent collectible balances from developers for loans under Community Development Block Grant and Housing and Urban Development programs.

11. Capital Assets

Capital asset activity for the year ended June 30, 2010 was as follows (in thousands):

| | <u>Beginning Balance</u> | <u>Increases</u> | <u>Decreases</u> | <u>Ending Balance</u> |
|--|------------------------------|------------------|------------------|---------------------------|
| Governmental Activities: | | | | |
| Capital assets, being depreciated: | | | | |
| Land improvements | \$ 6,993 | \$ 110 | \$ - | \$ 7,103 |
| Construction | 107,534 | 86 | - | 107,620 |
| Infrastructure | 22,943 | 853 | - | 23,796 |
| Machinery and equipment | 10,076 | 162 | (533) | 9,705 |
| Licenses and vehicles | <u>9,170</u> | <u>418</u> | <u>-</u> | <u>9,588</u> |
| Total capital assets, being depreciated | 156,716 | 1,629 | (533) | 157,812 |
| Less accumulated depreciation for: | | | | |
| Land improvements | (4,255) | (227) | - | (4,482) |
| Construction | (43,663) | (2,080) | - | (45,743) |
| Infrastructure | (16,121) | (564) | - | (16,685) |
| Machinery and equipment | (8,773) | (269) | 517 | (8,525) |
| Licenses and vehicles | <u>(8,088)</u> | <u>(300)</u> | <u>-</u> | <u>(8,388)</u> |
| Total accumulated depreciation | <u>(80,900)</u> | <u>(3,440)</u> | <u>517</u> | <u>(83,823)</u> |
| Total capital assets, being depreciated, net | 75,816 | (1,811) | (16) | 73,989 |
| Capital assets, not being depreciated: | | | | |
| Land, easements and right of way | 9,210 | - | - | 9,210 |
| Construction in progress | <u>136</u> | <u>1,520</u> | <u>-</u> | <u>1,656</u> |
| Total capital assets, not being depreciated | <u>9,346</u> | <u>1,520</u> | <u>-</u> | <u>10,866</u> |
| Governmental activities capital assets, net | <u>\$ 85,162</u> | <u>\$ (291)</u> | <u>\$ (16)</u> | <u>\$ 84,855</u> |

| | <u>Beginning Balance</u> | <u>Increases</u> | <u>Decreases</u> | <u>Ending Balance</u> |
|--|------------------------------|------------------|------------------|---------------------------|
| Business-Type Activities: | | | | |
| Capital assets, being depreciated: | | | | |
| Land improvements | \$ 218 | \$ - | \$ - | \$ 218 |
| Construction | 22,801 | 11,600 | - | 34,401 |
| Infrastructure | 25,787 | 225 | - | 26,012 |
| Machinery and equipment | 2,535 | - | (9) | 2,526 |
| Licenses and vehicles | 258 | 194 | - | 452 |
| | <u>258</u> | <u>194</u> | <u>-</u> | <u>452</u> |
| Total capital assets, being depreciated | 51,599 | 12,019 | (9) | 63,609 |
| Less accumulated depreciation for: | | | | |
| Land improvements | (205) | (3) | - | (208) |
| Construction | (5,193) | (423) | - | (5,616) |
| Infrastructure | (15,733) | (261) | - | (15,994) |
| Machinery and equipment | (1,539) | (78) | 9 | (1,608) |
| Licenses and vehicles | (148) | (43) | - | (191) |
| | <u>(148)</u> | <u>(43)</u> | <u>-</u> | <u>(191)</u> |
| Total accumulated depreciation | (22,818) | (808) | 9 | (23,617) |
| Total capital assets, being depreciated, net | 28,781 | 11,211 | - | 39,992 |
| Capital assets, not being depreciated: | | | | |
| Land, easements & right of way | 252 | - | - | 252 |
| Construction in progress | 11,485 | - | (11,485) | - |
| | <u>11,485</u> | <u>-</u> | <u>(11,485)</u> | <u>-</u> |
| Total capital assets, not being depreciated | 11,737 | - | (11,485) | 252 |
| Business-type activities capital assets, net | \$ 40,518 | \$ 11,211 | \$ (11,485) | \$ 40,244 |

Depreciation expense was charged to functions of the City as follows (in thousands):

Governmental Activities:

| | |
|--|----------|
| General government | \$ 172 |
| Public safety | 199 |
| Education | 2,259 |
| Public works | 810 |
| Total depreciation expense - governmental activities | \$ 3,440 |

Business-Type Activities:

| | |
|------------|---------------|
| Enterprise | \$ <u>807</u> |
|------------|---------------|

12. Warrants and Accounts Payable

Warrants payable represent 2010 expenditures paid by July 15, 2010 as permitted by law. Accounts payable represent additional 2010 expenditures paid after July 15, 2010.

13. Accrued Liabilities

The City had the following accrued liabilities as of June 30, 2010:

| | <u>Governmental</u> | <u>Business-Type</u> |
|---------------------------|---------------------|----------------------|
| Salaries and wages | \$ 1,207,232 | \$ 72,724 |
| Debt interest | 477,480 | 267,523 |
| Tailings | <u>158,911</u> | <u>2,121</u> |
| Total accrued liabilities | <u>\$ 1,843,623</u> | <u>\$ 342,368</u> |

14. Deferred Revenue

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period.

The balance of the General Fund deferred revenues account is equal to the total of all June 30, 2010 receivable balances, except real and personal property taxes that are accrued for subsequent 60 day collections.

15. Loan and Anticipation Notes Payable

The City had the following notes outstanding at June 30, 2010:

| | Interest Rate | Date of Issue | Date of Maturity | Balance at 6/30/10 |
|--------------------------------------|------------------|------------------|---------------------|-----------------------|
| Recreation - High School Track | 1.90% | 08/14/09 | 08/13/10 | \$ 210,000 |
| Water Treatment Plant Improvement | 1.76% | 04/01/09 | 07/15/10 | 626,593 |
| Methuen High School Revitalization | 2.00% | 05/21/10 | 05/20/11 | 1,000,000 |
| Stormwater Management | 2.00% | 05/21/10 | 05/20/11 | <u>12,243</u> |
| Total | | | | <u>\$ 1,848,836</u> |

The following summarizes activity in notes payable during fiscal year 2010:

| | Balance Beginning of Year | New Issues | Maturities | Balance End of Year |
|---------------------------------------|---------------------------------|---------------------|-----------------------|---------------------------|
| Recreation | \$ 230,000 | \$ 210,000 | \$ (230,000) | \$ 210,000 |
| Water treatment plant improvements | 512,264 | 114,329 | - | 626,593 |
| High School Revitalization | 1,000,000 | 1,000,000 | (1,000,000) | 1,000,000 |
| Stormwater Management | - | 12,243 | - | 12,243 |
| Revenue Anticipation | - | 4,500,000 | (4,500,000) | - |
| Total | \$ 1,742,264 | \$ 5,836,572 | \$ (5,730,000) | \$ 1,848,836 |

16. Other Current Liabilities

Other current liabilities as of June 30, 2010 consist of the following:

| | |
|--|---------------------|
| IBNR (see note 26) | \$ 1,115,809 |
| Guaranteed deposits | 973,002 |
| Employee withholdings and other | <u>117,879</u> |
| Total other current liabilities | \$ 2,206,690 |

17. Capital Lease Obligations

The City's outstanding lease agreements include the acquisition of computers, fire trucks, highway trucks, police vehicles and a communication system. These leases qualify as capital leases. Future minimum lease payments under the capital leases consisted of the following as of June 30, 2010:

| | Governmental Activities | Business-Type Activities |
|--|----------------------------|-----------------------------|
| 2011 | \$ 216,181 | \$ 42,942 |
| 2012 | 62,742 | 42,942 |
| 2013 | 62,742 | 42,942 |
| 2014 | 62,742 | 42,942 |
| Total minimum lease payments | 404,407 | 171,768 |
| Less amount representing interest | (32,450) | (19,846) |
| Present Value of Minimum Lease Payments | \$ 371,957 | \$ 151,922 |

The following is an analysis for the leased assets included in capital assets at June 30, 2010:

| | <u>Governmental Activities</u> | <u>Business-Type Activities</u> |
|-------------------------------------|--------------------------------|---------------------------------|
| Machinery, vehicles and equipment | \$ 1,095,304 | \$ 194,044 |
| Less: accumulated depreciation | <u>(404,371)</u> | <u>(10,878)</u> |
| Equipment under capital leases, net | <u>\$ 690,933</u> | <u>\$ 183,166</u> |

18. Long-Term Debt

A. Long-Term Debt Supporting Activities

The City issues general obligation bonds to provide funds for the acquisition, construction, and improvements of major capital facilities and infrastructure. General obligation bonds have been issued for both governmental and business-type activities and are repaid with general and enterprise fund revenues. Compensated absences are paid from the fund responsible for the employee's compensation with significant liabilities paid from general fund and the rest from enterprise fund. Landfill closure costs are paid from general fund, and capital lease payments are made from general and enterprise funds.

B. General Obligation Bonds and Other Long-Term Debt

General obligation bonds and loans currently outstanding are as follows:

| <u>Governmental Activities:</u> | <u>Original Issue Amount</u> | <u>Serial Maturities Through</u> | <u>Interest Rate(s)%</u> | <u>Amount Outstanding as of 6/30/10</u> |
|---------------------------------|------------------------------|----------------------------------|--------------------------|---|
| Recreation | \$ 253,600 * | 11/01/11 | 4.80% | \$ 32,000 |
| Recreation | 1,600,000 * | 11/01/12 | 5.01% | 315,000 |
| Marsh School Expansion | 17,399,400 * | 11/01/16 | 4.80% | 8,313,000 |
| Timony School Expansion | 21,190,000 * | 11/01/16 | 5.01% | 10,340,000 |
| Landfill Closure | 3,500,000 * | 11/01/16 | 5.01% | 1,305,000 |
| Tenney School Expansion | 22,850,000 * | 05/15/17 | 4.79% | 11,180,000 |
| Additional School Expansion | 6,500,000 * | 10/15/19 | 5.00% | 3,530,000 |
| Library | 4,800,000 * | 10/15/19 | 5.00% | 2,595,000 |

(continued)

(continued)

| | Original Issue <u>Amount</u> | Serial Maturities <u>Through</u> | Interest <u>Rate(s)%</u> | Amount Outstanding as of <u>6/30/10</u> |
|--|------------------------------------|--|-----------------------------|--|
| <u>Governmental Activities:</u> | | | | |
| Road and Surface Drains | 5,630,000 | 09/01/21 | 3.27% | 2,140,000 |
| Landfill Closure | 85,000 | 09/01/21 | 3.91% | 60,000 |
| Road and Surface Drains | 3,500,000 | 08/15/16 | 4.30% | 2,500,000 |
| Dileo Judgment | 600,000 | 08/14/10 | 1.90% | <u>600,000</u> |
| Total Governmental Activities | | | | \$ <u>42,910,000</u> |

| | Original Issue <u>Amount</u> | Serial Maturities <u>Through</u> | Interest <u>Rate(s)%</u> | Amount Outstanding as of <u>6/30/10</u> |
|---|------------------------------------|--|-----------------------------|--|
| <u>Business-Type Activities:</u> | | | | |
| Sewer | \$ 821,670 * | 02/01/15 | variable | \$ 293,439 |
| Sewer | 395,100 * | 08/01/18 | variable | 266,101 |
| Storm Water Management | 468,063 * | 08/01/23 | variable | 358,021 |
| Water Distribution System | 5,786,500 * | 07/15/25 | 2.00% | 4,826,433 |
| Storm Water Management | 200,000 * | 07/15/27 | 2.00% | 170,752 |
| Water Distribution System | 18,550,000 * | 07/15/27 | 2.00% | 17,036,026 |
| Water Treatment Plant | 1,250,000 | 08/15/28 | 4.16% | 1,170,000 |
| Water Distribution System | 700,000 | 08/15/28 | 4.16% | 655,000 |
| Water Tank | 750,000 * | 07/15/27 | 2.00% | 449,593 |
| Sewer Rehabilitation and Replacement | 1,117,204 * | 01/28/28 | 2.00% | <u>1,067,604</u> |
| Total Business-Type Activities | | | | \$ <u>26,292,969</u> |

*Registered owner of these bonds is the Massachusetts Water Pollution Abatement Trust.

C. Future Debt Service

The annual payments to retire all general obligation long-term debt outstanding as of June 30, 2010 are as follows:

| <u>Governmental</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|---------------------|----------------------|---------------------|----------------------|
| 2011 | \$ 7,055,000 | \$ 1,695,187 | \$ 8,750,187 |
| 2012 | 6,560,000 | 1,402,325 | 7,962,325 |
| 2013 | 6,360,000 | 1,110,231 | 7,470,231 |
| 2014 | 6,080,000 | 838,301 | 6,918,301 |
| 2015 | 5,830,000 | 586,693 | 6,416,693 |
| 2016-2020 | 10,925,000 | 550,556 | 11,475,556 |
| 2021-2025 | <u>100,000</u> | <u>4,275</u> | <u>104,275</u> |
| Total | <u>\$ 42,910,000</u> | <u>\$ 6,187,568</u> | <u>\$ 49,097,568</u> |

| <u>Business-Type</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|----------------------|----------------------|---------------------|----------------------|
| 2011 | \$ 1,298,312 | \$ 587,199 | \$ 1,885,511 |
| 2012 | 1,325,473 | 557,587 | 1,883,060 |
| 2013 | 1,339,326 | 533,271 | 1,872,597 |
| 2014 | 1,386,904 | 496,788 | 1,883,692 |
| 2015 | 1,422,623 | 464,746 | 1,887,369 |
| 2016-2020 | 7,242,944 | 1,831,854 | 9,074,798 |
| 2021-2025 | 7,872,667 | 968,993 | 8,841,660 |
| 2026-2030 | <u>4,404,720</u> | <u>151,231</u> | <u>4,555,951</u> |
| Total | <u>\$ 26,292,969</u> | <u>\$ 5,591,669</u> | <u>\$ 31,884,638</u> |

D. Bond Authorizations

Long-term debt authorizations which have not been issued or rescinded as of June 30, 2010 are as follows:

| <u>Date Authorized</u> | <u>Purpose</u> | <u>Amount</u> |
|------------------------|--|-----------------------|
| 09/10/05 | Recreation - High School Track | \$ 210,000 |
| 06/17/09 | Water Treatment Plant Improvement | 650,000 |
| 04/02/09 | Methuen High School Revitalization | 2,000,000 |
| 07/05/06 | Sewer rehab and East Capital St. project | 202,796 |
| 07/05/06 | Stormwater Management | 12,924 |
| 06/15/10 | Methuen High School | <u>99,100,000</u> |
| Total | | <u>\$ 102,175,720</u> |

E. Changes in General Long-Term Liabilities

During the year ended June 30, 2010, the following changes occurred in long-term liabilities (in thousands):

| | Total Balance 7/1/09 | Additions | Restructuring | Reductions | Total Balance 6/30/10 | Less Current Portion | Equals Long-Term Portion 6/30/10 |
|-------------------------------------|----------------------------|------------------|-----------------|--------------------|-----------------------------|----------------------------|---|
| Governmental Activities | | | | | | | |
| General obligation debt | \$ 48,650 | \$ 600 | \$ - | \$ (6,340) | \$ 42,910 | \$ (7,055) | \$ 35,855 |
| Net OPEB obligation | 9,594 | 13,974 | - | (4,379) | 19,189 | - | 19,189 |
| Other: | | | | | | | |
| Capital leases | 660 | - | - | (288) | 372 | (195) | 177 |
| Landfill closure | 760 | - | - | (40) | 720 | (40) | 680 |
| Accrued employee benefits | 3,390 | 169 | - | - | 3,559 | (1,780) | 1,779 |
| Totals | <u>\$ 63,054</u> | <u>\$ 14,743</u> | <u>\$ -</u> | <u>\$ (11,047)</u> | <u>\$ 66,750</u> | <u>\$ (9,070)</u> | <u>\$ 57,680</u> |
| Business-Type Activities | | | | | | | |
| General obligation debt | \$ 27,827 | \$ - | \$ (252) | \$ (1,282) | \$ 26,293 | \$ (1,298) | \$ 24,995 |
| Net OPEB obligation | 252 | 368 | - | (116) | 504 | - | 504 |
| Other: | | | | | | | |
| Capital leases | - | 194 | - | (42) | 152 | (35) | 117 |
| Accrued employee benefits | 175 | 9 | - | - | 184 | - | 184 |
| Totals | <u>\$ 28,254</u> | <u>\$ 571</u> | <u>\$ (252)</u> | <u>\$ (1,440)</u> | <u>\$ 27,133</u> | <u>\$ (1,333)</u> | <u>\$ 25,800</u> |

General obligation bonds, issued by the City for various municipal projects, are approved by City Council and repaid with revenues from the General Fund. Compensated absences are repaid from the funds that the costs relate to, mostly general fund and also enterprise fund. Landfill closure costs are repaid from general fund revenues. Capital leases are repaid with general fund and special revenue fund revenues.

F. Prior Year Defeasance of Debt

In prior years, certain outstanding bonds were defeased by placing proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust accounts and the defeased bonds are not included in the financial statements.

Defeased debt still outstanding at June 30, 2010 is \$ 8,265,000.

19. Subsequent Events

Debt

The City issued a revenue anticipation note dated July 1, 2010 in the amount of \$ 7,500,000 maturing July 1, 2011 with an interest rate of 1.32%.

Health Insurance Deficit

The June 30, 2010 health insurance appropriation deficit of \$ 3,335,453 was funded subsequent to year end by \$1,440,000 transfer from Stabilization Fund, \$1,374,456 from fiscal year 2011 school department budget, and \$ 520,997 from fiscal year 2011 tax levy and budget savings from early retirement. A Home Rule petition has been filed with the State House to allow borrowing up to \$ 1,960,997. If the Home Rule petition passes, the City intends to reimburse the Stabilization Fund.

20. Landfill Closure and Postclosure Care Costs

State and Federal laws and regulations require the City to place a final cover on its landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for thirty years after closure.

The \$ 720,000 is reported as landfill postclosure care liability at June 30, 2010. Actual cost may be higher due to inflation, changes in technology, or changes in regulations.

21. Restricted Net Assets

The accompanying entity-wide financial statements report restricted net assets when external constraints from grantors or contributors are placed on net assets.

Permanent fund restricted net assets are segregated between nonexpendable and expendable. The nonexpendable portion represents the original restricted principal contribution, and the expendable represents accumulated earnings which are available to be spent based on donor restrictions.

22. Reserves of Fund Equity

“Reserves” of fund equity are established to segregate fund balances which are either not available for expenditure in the future or are legally set aside for a specific future use.

The following types of reserves are reported at June 30, 2010:

Reserved for Encumbrances - An account used to segregate that portion of fund balance committed for expenditure of financial resources upon vendor performance.

Reserved for Other Purposes - An account used to segregate that portion of fund balance committed for potential contributions needed to fund Chapter 90 and Police Weed and Seed grant deficit balances.

Reserved for Perpetual Funds - Represents the principal of the nonexpendable trust fund investments. The balance cannot be spent for any purpose; however, it may be invested and the earnings may be spent.

23. Commitments and Contingencies

Outstanding Lawsuits - There are several pending lawsuits in which the City is involved. The City's management is of the opinion that the potential future settlement of such claims would not materially affect its financial statements taken as a whole.

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

24. Post-Employment Health Care and Life Insurance Benefits

Other Post-Employment Benefits

GASB Statement 45, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions*, requires governments to account for other post-employment benefits (OPEB), primarily healthcare, on an accrual basis rather than on a pay-as-you-go basis. The effect is the recognition of an actuarially required contribution as an expense on the statement of revenues, expenses, and changes in net assets when a future retiree earns their post-employment benefits, rather than when they use their post-employment benefit. To the extent that an entity does not fund their actuarially required contribution, a post-employment benefit liability is recognized on the Statement of Net Assets over time.

A. Plan Description

In addition to providing the pension benefits described, the City provides post-employment health care and life insurance benefits for retired employees through the City's plan. The benefits, benefit levels, employee contributions

and employer contributions are governed by Chapter 32 of the Massachusetts General Laws. As of June 30, 2008, the actuarial valuation date, approximately 763 retirees and 794 active employees meet the eligibility requirements. The plan does not issue a separate financial report.

B. Benefits Provided

The City provides medical, prescription drug, mental health/substance abuse and life insurance to retirees and their covered dependents. All active employees who retire from the City and meet the eligibility criteria will receive these benefits.

C. Funding Policy

Medicare retirees contribute 20% and Tufts or Blue Cross retirees contribute 38% of the cost of the health plan, as determined by the City. The City contributes the remainder of the health plan costs on a pay-as-you-go basis.

D. Annual OPEB Costs and Net OPEB Obligation

The City's fiscal 2010 annual OPEB expense is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost per year and amortize the unfunded actuarial liability over a period of thirty years. The following table shows the components of the City's annual OPEB cost for the year ending June 30, 2010, the amount actually contributed to the plan, and the change in the City's net OPEB obligation based on an actuarial valuation as of June 30, 2008.

| | |
|---|----------------------|
| Annual Required Contribution (ARC) | \$ 14,340,252 |
| Interest on net OPEB obligation | - |
| Adjustment to ARC | - |
| Annual OPEB cost | 14,340,252 |
| Contributions made | <u>(4,493,986)</u> |
| Increase in net OPEB obligation | 9,846,266 |
| Net OPEB obligation - beginning of year | <u>9,846,266</u> |
| Net OPEB obligation - end of year | \$ <u>19,692,532</u> |

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

| Fiscal year ended | Annual OPEB Cost | Percentage of OPEB Cost Contributed | | Net OPEB Obligation |
|-------------------|---------------------|---|-------|------------------------|
| | | Cost Contributed | 31.3% | |
| 2010 | \$ 14,340,252 | | 31.3% | \$ 19,692,532 |
| 2009 | \$ 14,340,252 | | 31.3% | \$ 9,846,266 |

E. Funded Status and Funding Progress

The funded status of the plan as of June 30, 2008, the date of the most recent actuarial valuation was as follows:

| | |
|---|-----------------------|
| Actuarial accrued liability (AAL) | \$ 209,816,378 |
| Actuarial value of plan assets | <u>-</u> |
| Unfunded actuarial accrued liability (UAAL) | \$ <u>209,816,378</u> |
| Funded ratio (actuarial value of plan assets/AAL) | <u>0%</u> |
| Covered payroll (active plan members) | \$ <u>80,056,909</u> |
| UAAL as a percentage of covered payroll | <u>262.1%</u> |

Actuarial valuations of an ongoing plan involve estimates of the value of reported amount and assumptions about the probability of occurrence of events far into the future. Examples included assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

F. Actuarial Methods and Assumptions

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

In the June 30, 2008 actuarial valuation the projected unit credit cost method was used. The actuarial value of assets was not determined as the City has not advance funded its obligation. The actuarial assumptions included a 4.5% investment rate of return and an initial annual healthcare cost trend rate of 10% which decreases to a 5% long-term rate for all healthcare benefits after ten years. The amortization costs for the initial UAAL is a level percentage of payroll for a period of 30 years, on an open basis. This has been calculated assuming the amortization payment increases at a rate of 4.5%.

25. Contributory Retirement System

The City follows the provisions of GASB Statement No. 27, Accounting for Pensions for State and Local Government Employees, (as amended by GASB 50) with respect to the employees' retirement funds.

A. Plan Description and Contribution Information

Substantially all employees of the City (except teachers and administrators under contract employed by the School Department) are members of the Methuen Contributory Retirement System (MCRS), a cost sharing, multiple employer defined benefit PERS. Eligible employees must participate in the MCRS. The pension plan provides pension benefits, deferred allowances, and death and disability benefits. Chapter 32 of the Massachusetts General Laws establishes the authority of the MCRS Retirement Board. Chapter 32 also establishes contribution percentages and benefits paid. The MCRS Retirement Board does not have the authority to amend benefit provisions. As required by Massachusetts General Laws, the System issues a separate report to the Commonwealth's Public Employee Retirement Administration Commission.

Membership of each plan consisted of the following at December 31, 2009:

| | |
|--|---------------------|
| Retirees and beneficiaries receiving benefits | 404 |
| Terminated plan members entitled to but not yet receiving benefits | 94 |
| Active plan members | <u>634</u> |
| Total | <u><u>1,132</u></u> |
| Number of participating employers | 2 |

Employee contribution percentages are specified in Chapter 32 of the Massachusetts General Laws. The percentage is determined by the participant's date of entry into the system. All employees hired after January 1, 1979 contribute an additional 2% on all gross regular earnings over the rate of \$ 30,000 per year. The percentages are as follows:

| | |
|-------------------------------------|----|
| Before January 1, 1975 | 5% |
| January 1, 1975 - December 31, 1983 | 7% |
| January 1, 1984 - June 30, 1996 | 8% |
| Beginning July 1, 1996 | 9% |

Employers are required to contribute at actuarially determined rates as accepted by the Public Employee Retirement Administration Commission (PERAC). The City's Schedule of Employer Contributions is as follows:

| Year Ended <u>June 30</u> | Annual Required <u>Contribution</u> | Percentage <u>Contributed</u> |
|------------------------------|--|----------------------------------|
| 2001 | \$ 2,572,051 | 100% |
| 2002 | 2,674,933 | 100% |
| 2003 | 2,772,000 | 100% |
| 2004 | 2,244,581 | 100% |
| 2005 | 3,186,100 | 100% |
| 2006 | 4,966,000 | 100% |
| 2007 | 5,160,000 | 100% |
| 2008 | 5,362,000 | 100% |
| 2009 | 6,000,000 | 100% |
| 2010 | 6,600,000 | 100% |

B. Summary of Significant Accounting Policies

Basis of Accounting - Contributory retirement system financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Method Used to Value Investments - Investments are reported at fair value in accordance with PERAC requirements.

C. Funded Status and Funding Progress

The information presented below is from the Methuen Contributory Retirement System's most recent valuation.

| Actuarial Valuation Date | Actuarial Value of Assets | Actuarial Accrued Liability | | | Unfunded AAL (UAAL) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll [(b-a)/c] |
|--------------------------|---------------------------|-----------------------------|---------------|-------|---------------------|--------------------|---------------------|---|
| | | (a) | (b) | (b-a) | | | | |
| 01/01/08 | \$ 87,315,553 | \$ 154,331,693 | \$ 67,016,140 | 56.6% | \$ 30,100,933 | | | 222.6% |

The Schedule of Funding Progress following the notes to the financial statements presents multi-year trend information about the actuarial value of plan assets relative to the actuarial accrued liability for benefits.

D. Actuarial Methods and Assumptions

The annual required contribution for the current year was determined as part of the actuarial valuation using the entry age normal actuarial cost method. Under this method an unfunded actuarial accrued liability of \$ 67 million was calculated. The actuarial assumptions included (a) 8% investment rate of return and (b) a projected salary increase of 4.75 - 5.25% per year. Liabilities for cost of living increases have been assumed at an annual increase of 3%, on the first \$ 12,000 of benefit payments. The actuarial value of assets is determined by projecting the market value of assets as of the beginning of the prior plan year with the assumed rate of return during that year (8%) and accounting for deposits and disbursements with interest at the assumed rate of return. An adjustment is then applied to recognize the difference between the actual investment return and expected return over a five-year period. As of December 31, 2008, the unfunded actuarially accrued liability is being amortized over 19 years using a 4.5% increasing payment method.

E. Teachers

As required by State statutes, teachers of the City are covered by the Massachusetts Teachers Retirement System (MTRS). The MTRS is funded by contributions from covered employees and the Commonwealth of Massachusetts. The City is not required to contribute.

All persons employed on at least a half-time basis, who are covered under a contractual agreement requiring certification by the Board of Education are eligible, and must participate in the MTRS.

Based on the Commonwealth of Massachusetts' retirement laws, employees covered by the pension plan must contribute a percentage of gross earnings into the pension fund. The percentage is determined by the participant's date of entry into the system and gross earnings, up to \$ 30,000, as follows:

| | |
|-------------------------------------|------|
| Before January 1, 1975 | 5% |
| January 1, 1975 - December 31, 1983 | 7% * |
| January 1, 1984 - June 30, 1996 | 8% * |
| July 1, 1996 - June 30, 2001 | 9% * |
| Beginning July 1, 2001 | 11% |

*Effective January 1, 1990, all participants hired after January 1, 1979, who have not elected to increase to 11%, contribute an additional 2% of salary in excess of \$ 30,000.

The City's current year covered payroll for teachers and administrators was \$ 38,802,258.

In fiscal year 2010, the Commonwealth of Massachusetts contributed \$ 8,889,711 to the MTRS on behalf of the City. This is included in the education expenditures and intergovernmental revenues in the general fund.

26. Self Insurance

The City self insures for health coverage. Annual estimated requirements for claims are provided in the City's annual operating budget. The City contracts with an insurance carrier for excess liability coverage and an insurance consultant for claims processing. Under the terms of its insurance coverage, the City is liable for claims up to \$ 125,000 per incident. The claims liability represents an estimate of claims incurred but unpaid at year-end, based on past historical costs and claims paid subsequent to year-end.

Changes in the aggregate liability for claims for the year ended June 30, 2010 are as follows (also see note 1k):

| | <u>Year Ended</u> <u>June 30, 2010</u> | <u>Year Ended</u> <u>June 30, 2009</u> |
|---|---|---|
| Unpaid claims, beginning of fiscal year | \$ 791,582 | \$ 1,843,015 |
| Claims incurred (including IBNRs) | 18,772,977 | 15,147,308 |
| Claims paid | <u>(18,448,750)</u> | <u>(16,198,741)</u> |
| Unpaid claims, end of fiscal year | <u>\$ 1,115,809 *</u> | <u>\$ 791,582 *</u> |

* This liability is considered to be all current.

The \$ 1,115,809 estimated liability for claims incurred but not reported includes only an estimate for known loss events expected to later be presented as claims. The City is unable to estimate the amount of unknown loss events expected to become claims and expected future developments on claims already reported.

27. 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; and natural disasters for which the government carries commercial insurance. There were no significant reductions in insurance coverage from the previous year and have been no material settlements in excess of coverage in any of the past three fiscal years.

CITY OF METHUEN, MASSACHUSETTS
SCHEDULE OF FUNDING PROGRESS
REQUIRED SUPPLEMENTARY INFORMATION

June 30, 2010

(Unaudited)

Employees' Retirement System

| Actuarial Valuation Date | Actuarial Value of Assets <u>(a)</u> | Actuarial Accrued Liability (AAL) - Entry Age <u>(b)</u> | Unfunded AAL (UAAL) <u>(b-a)</u> | Funded Ratio <u>(a/b)</u> | Covered Payroll <u>(c)</u> | UAAL as a Percent- age of Covered Payroll <u>[(b-a)/c]</u> |
|--------------------------------|---|---|---|---------------------------------|----------------------------------|---|
| 01/01/08 | \$ 87,315,553 | \$ 154,331,693 | \$ 67,016,140 | 56.6% | \$ 30,100,933 | 222.6% |
| 01/01/07 | \$ 79,875,823 | \$ 146,337,558 | \$ 66,461,735 | 54.6% | \$ 29,257,209 | 227.2% |
| 01/01/04 | \$ 71,932,860 | \$ 117,599,583 | \$ 45,666,723 | 61.2% | \$ 25,933,704 | 176.1% |
| 01/01/01 | \$ 68,625,708 | \$ 92,496,265 | \$ 23,870,557 | 74.2% | \$ 22,480,573 | 106.2% |
| 01/01/97 | \$ 42,617,519 | \$ 66,863,478 | \$ 24,245,959 | 63.7% | \$ 16,295,087 | 148.8% |
| 01/01/96 | \$ 37,886,763 | \$ 58,261,376 | \$ 20,374,613 | 65.0% | \$ 15,520,687 | 131.3% |
| 01/01/93 | \$ 25,970,674 | \$ 45,965,677 | \$ 19,995,003 | 56.5% | \$ 14,905,887 | 134.1% |

Other Post-Employment Benefits

| Actuarial Valuation Date | Actuarial Value of Assets <u>(a)</u> | Actuarial Accrued Liability (AAL) - Entry Age <u>(b)</u> | Unfunded AAL (UAAL) <u>(b-a)</u> | Funded Ratio <u>(a/b)</u> | Covered Payroll <u>(c)</u> | UAAL as a Percent- age of Covered Payroll <u>[(b-a)/c]</u> |
|--------------------------------|---|---|---|---------------------------------|----------------------------------|---|
| 06/30/08 | \$ - | \$ 209,816,378 | \$ 209,816,378 | 0.0% | \$ 80,056,909 | 262.1% |

See Independent Auditors' Report.