

CITY OF SALEM, MASSACHUSETTS

**REPORT ON EXAMINATION OF
GENERAL PURPOSE FINANCIAL STATEMENTS
AND ADDITIONAL INFORMATION
YEAR ENDED JUNE 30, 1998
AND
INDEPENDENT AUDITOR'S REPORT**

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INFORMATION
YEAR ENDED JUNE 30, 1998**

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TUCCI & ROSELLI

CERTIFIED PUBLIC ACCOUNTANTS
MANAGEMENT CONSULTANTS

INDEPENDENT AUDITORS' REPORT

To the City Council and Mayor
City of Salem, Massachusetts

We have audited the accompanying general purpose financial statements of the City of Salem, Massachusetts, as of and for the year ended June 30, 1998, as listed in the accompanying table of contents, except for the Pension Trust Fund which is as of and for the year ended December 31, 1997. These general purpose financial statements are the responsibility of the City of Salem's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

Except as discussed in the following two paragraphs, we conducted our audit in accordance with generally accepted auditing standards and *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 general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Governmental Accounting Standards Board Technical Bulletin 98-1, *Disclosures about Year 2000 Issues*, requires disclosure of certain matters regarding the year 2000 issue. The City of Salem, Massachusetts, has included such disclosures in Note 11. Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Accordingly, insufficient audit evidence exists to support the City of Salem, Massachusetts', disclosures with respect to the year 2000 issue made in Note 11. Further, we do not provide assurance that the City of Salem, Massachusetts', year 2000 remediation efforts will be successful in whole or in part, or that parties with which the City of Salem, Massachusetts, does business, will be year 2000 ready.

The City does not maintain adequate records with respect to its health claims activity. Accordingly, we were unable to determine the accurate cash and equity balances with respect to this activity. As such, we do not provide assurance that these cash and equity balances reflected in the financial statements are fairly presented.

The general purpose financial statements referred to above do not include a statement of general fixed assets, which should be included to conform with generally accepted accounting principles. Inasmuch as the Commonwealth of Massachusetts does not require, and the City has not capitalized fixed assets, the amount that should be recorded in the general fixed asset account group is not known.

As more fully described in Note 2 (c), the City maintains their enterprise funds on a comprehensive basis of accounting other than generally accepted accounting principles. Accordingly, the enterprise funds are not intended to present the financial position and results of operations in conformity with generally accepted accounting principles.

As discussed in Note 12, the City has not disclosed all required Pension Trust Fund disclosures necessary to be in accordance with generally accepted accounting principles.

As more fully described in Note 13, the City accounts for its risk financing activities on a comprehensive basis of accounting other than generally accepted accounting principles. Accordingly, the recognition of this activity is not intended to present the financial position and results of operation in conformity with generally accepted accounting principles.

In our opinion, except for the effects on the financial statements of the matters described in the preceding six paragraphs, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the City of Salem, Massachusetts, at June 30, 1998, except for the Pension Trust Fund which is as of and for the year ended December 31, 1997, and the results of its operations and cash flows of its nonexpendable trust funds and proprietary fund types for the year then ended, in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 30, 1998, which includes instances of material weaknesses, on our consideration of the City of Salem's internal control structure and its compliance with laws and regulations.

Our audit was conducted for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The statistical section, which is not a required part of the general purpose financial statements, but presented for additional analysis and the required supplementary information is also the responsibility of the City's management, and in our opinion, except for the effect of matters described in paragraphs three through eight is fairly stated in all material respects when considered in relation to the general purpose financial statements taken as a whole.



Tucci & Roselli
Certified Public Accountants
October 30, 1998

CITY OF SALEM, MASSACHUSETTS
COMBINED BALANCE SHEET - ALL FUND TYPES AND ACCOUNT GROUP
JUNE 30, 1998

(Except for the Pension Trust which is for the year ended December 31, 1997)
(General Fund 1997 amounts are shown for comparative purposes only.)

	Governmental Fund Types					Fiduciary Fund Types		Proprietary Fund Type	Account Group
	General Fund		Special Revenue Funds	Capital Projects Funds	Trust and Agency Funds	Pension Trust Fund	Enterprise Fund	General Long-Term Obligations	
	1998	1997							
								Combined Total (Memorandum Only)	
ASSETS AND OTHER DEBITS									
Cash and equivalents	\$9,404,931	\$5,637,273	\$693,153	\$36,679	\$2,762,878	\$903,570	\$927,448		\$14,728,659
Investments:									
Investments					4,726,001	55,319,949			60,045,950
Investment in deferred compensation plan					6,988,482				6,988,482
Receivables:									
Property taxes (Note 4)	942,495	1,822,954							942,495
Other (Note 7)	2,875,134	2,327,557	5,253,657		219,088	2,317,147			10,665,026
Water and sewer user charges							1,639,369		1,639,369
Due from other government	369,446		2,464,816						2,834,262
Other assets	204,765	277,195					535,207		739,972
Amount to be provided for retirement of general long-term obligations								\$40,608,193	40,608,193
Total assets and other debits	\$13,796,771	\$10,064,979	\$8,411,626	\$36,679	\$14,696,449	\$58,540,666	\$3,102,024	\$40,608,193	\$139,192,408

See notes to general purpose financial statements.

CITY OF SALEM, MASSACHUSETTS
COMBINED BALANCE SHEET - ALL FUND TYPES AND ACCOUNT GROUP
JUNE 30, 1998

(Except for the Pension Trust which is for the year ended December 31, 1997)
(General Fund 1997 amounts are shown for comparative purposes only.)

	Governmental Fund Types				Fiduciary Fund Types		Proprietary Fund Type	Account Group
	General Fund		Special Revenue	Capital Projects	Trust and Agency	Pension	Enterprise	General Long-Term
	1998	1997	Funds	Funds	Funds	Trust Fund	Fund	Obligations
LIABILITIES, FUND EQUITY AND OTHER CREDITS								Combined Total (Memorandum Only)
Warrants and accounts payable								
Accrued expenses	\$2,513,095	\$2,542,015	\$680,396	\$27,444	\$481,665		\$60,994	\$3,763,594
Notes payable	1,099,841	716,585						1,099,841
Allowance for abatements				400,160				400,160
Other liabilities	105,067	117,500						105,067
Deferred revenues	1,113,714				532,393			1,646,107
Deferred compensation liability	3,386,878	3,985,037	5,253,657		6,988,482		1,639,369	10,279,904
Compensated absences								6,988,482
Bond indebtedness								2,038,193
								38,570,000
TOTAL LIABILITIES	8,218,595	7,361,137	5,934,053	427,604	8,002,540		1,700,363	64,891,348
FUND EQUITY (DEFICIT) AND OTHER CREDITS								
Reserved for encumbrances								424,173
Reserved for pension benefits	250,549	557,509					173,624	58,540,666
Reserved for health claims					494,473			494,473
Designated for special revenue			2,477,573					2,477,573
Designated for capital projects				(390,925)				(390,925)
Designated for expendable trust					2,542,623			2,542,623
Designated for nonexpendable trust					3,656,813			3,656,813
Retained earnings							1,228,037	1,228,037
Undesignated fund balances	5,327,627	2,146,333						5,327,627
Total fund equity (deficit)	5,578,176	2,703,842	2,477,573	(390,925)	6,693,909	58,540,666	1,401,661	74,301,060
Total liabilities, fund equity, and other credits	\$13,796,771	\$10,064,979	\$8,411,626	\$36,679	\$14,696,449	\$58,540,666	\$3,102,024	\$139,192,408

Concluded

See notes to general purpose financial statements.

CITY OF SALEM, MASSACHUSETTS
COMBINED STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES (DEFICIT)
ALL GOVERNMENTAL FUND TYPES AND EXPENDABLE TRUST FUNDS
YEAR ENDED JUNE 30, 1998
(General Fund 1997 amounts are shown for comparative purposes only.)

	Governmental Fund Types				Fiduciary Fund Types	
	General Fund		Special Revenue Funds	Capital Projects Funds	Expendable Trust Funds	Combined Total (Memorandum Only)
	1998	1997				
REVENUES:						
Real and personal property taxes, net	\$45,004,696	\$42,400,497				\$45,004,696
Motor vehicle and other excise	2,658,569	2,327,427				2,658,569
Intergovernmental	19,201,293	17,566,369	8,138,512			27,339,805
Departmental and other revenue	2,264,289	1,594,068	2,435,856	8,896		4,709,041
Licenses and permits	304,447	296,415				304,447
Fines and forfeitures	645,592	654,441				645,592
Investment income	540,904	294,782			\$72,751	613,655
Health claims contribution					4,885,540	4,885,540
Total revenues	70,619,790	65,133,999	10,574,368	8,896	4,958,291	86,161,345
EXPENDITURES:						
General government	3,937,660	4,078,734	771,469			4,709,129
Public safety	12,385,733	11,715,870	85,719			12,471,452
Education	30,608,062	28,139,366	3,600,187			34,208,249
Public works	3,775,469	4,208,451	1,028,625			4,804,094
Health and human services	543,433	549,015	342,875			886,308
Culture and recreation	2,398,642	2,308,523	171,437		12,784	2,582,863
Pension and fringe benefits	8,230,562	8,265,821				8,230,562
State and county assessments	1,887,916	1,842,397				1,887,916
Debt service:						
Principal	3,050,000	2,725,000				3,050,000
Interest	2,111,236	2,395,126				2,111,236
Health claims					5,687,078	5,687,078
Community development and capital outlay			2,813,361	1,909,687		4,723,048
Total expenditures	68,928,713	66,228,303	8,813,673	1,909,687	5,699,862	85,351,935
Excess (deficiency) of revenues over (under) expenditures	1,691,077	(1,094,304)	1,760,695	(1,900,791)	(741,571)	809,410
OTHER FINANCING SOURCES (USES):						
Operating transfers in	1,740,338	1,747,191	439,915	27,240	100,253	2,307,746
Operating transfers out	(557,081)	(34,939)	(1,133,875)			(1,690,956)
Total other financing sources (uses)	1,183,257	1,712,252	(693,960)	27,240	100,253	616,790
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other uses (Note 3)	2,874,334	617,948	1,066,735	(1,873,551)	(641,318)	1,426,200
FUND BALANCES, JULY 1, 1997	2,703,842	2,085,894	1,410,838	1,482,626	3,678,414	9,275,720
FUND BALANCES (DEFICIT), JUNE 30, 1998	\$5,578,176	\$2,703,842	\$2,477,573	(\$390,925)	\$3,037,096	\$10,701,920

See notes to general purpose financial statements.

**CITY OF SALEM, MASSACHUSETTS
STATEMENT OF REVENUES AND EXPENDITURES-
BUDGET AND ACTUAL - GENERAL FUND BUDGETARY BASIS
YEAR ENDED JUNE 30, 1998**

	Budget	Actual	Variance Favorable (Unfavorable)
REVENUES:			
Real and personal property taxes, net	\$43,311,030	\$43,396,059	\$85,029
Motor vehicle and other excise	2,045,000	2,658,569	613,569
Intergovernmental	18,852,041	19,201,293	349,252
Departmental and other revenue	2,122,443	2,264,288	141,845
Licenses and permits	290,000	304,447	14,447
Fines and forfeitures	600,000	645,592	45,592
Investment income	250,000	540,904	290,904
Total revenues	67,470,514	69,011,152	1,540,638
OTHER FINANCING SOURCES :			
Operating transfers (net)	1,582,615	1,582,615	0
Transfers from free cash	1,146,562	1,146,562	
Total other financing sources	2,729,177	2,729,177	0
Total revenue and other financing sources	70,199,691	71,740,329	1,540,638
EXPENDITURES:			
General government	4,238,734	3,996,799	241,935
Public safety	12,882,125	12,365,911	516,214
Education	30,273,033	30,275,222	(2,189)
Public works	4,294,891	3,756,722	538,169
Health and human services	557,468	543,433	14,035
Culture and recreation	2,516,199	2,303,952	212,247
Pension and fringe benefits	8,425,760	8,230,562	195,198
State and county assessments	1,818,927	1,887,916	(68,989)
Debt service	5,154,858	5,161,236	(6,378)
Prior year deficits	37,696		
Total expenditures	70,199,691	68,521,753	1,640,242
Excess of revenues and other financing sources over expenditures (Note 3)	\$0	\$3,218,576	

See notes to general purpose financial statements.

**CITY OF SALEM, MASSACHUSETTS
COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN
RETAINED EARNINGS / FUND BALANCES - NONEXPENDABLE TRUST FUNDS AND
PROPRIETARY FUND TYPES
YEAR ENDED JUNE 30, 1998**

	Proprietary Fund Type		Combined Total (Memorandum Only)
	Enterprise Fund	Nonexpendable Trust	
REVENUES:			
Charges for services	\$8,105,962		\$8,105,962
Investment income		\$518,180	518,180
Total revenues	8,105,962	518,180	8,624,142
EXPENSES:			
Operating expenses	7,324,508		7,324,508
Total expenses	7,324,508		7,324,508
Income before transfers	781,454	518,180	1,299,634
Other financing sources / (uses) - net Transfers to General Fund	(616,790)		(616,790)
NET INCOME	164,664	518,180	682,844
RETAINED EARNINGS / FUND EQUITY:			
July 1, 1997	1,236,997	1,770,197	3,007,194
Cumulative effect of change in accounting principle (Note 15)		1,368,436	1,368,436
June 30, 1998	\$1,401,661	\$3,656,813	\$3,690,038

See notes to general purpose financial statements.

**CITY OF SALEM, MASSACHUSETTS
COMBINED STATEMENT OF CASH FLOWS
NONEXPENDABLE TRUST FUNDS AND PROPRIETARY FUND TYPES
YEAR ENDED JUNE 30, 1998**

	<u>Proprietary Fund Type</u>		
	<u>Enterprise Fund</u>	<u>Nonexpendable Trust</u>	<u>Combined Total (Memorandum Only)</u>
CASH FLOWS FROM OPERATING ACTIVITIES AND NONOPERATING REVENUE:			
Net income from operations	\$164,664	\$518,180	\$682,844
Adjustments to reconcile net income from operations to net cash provided by operating activities:			
Effects of changes in assets and liabilities:			
Accounts receivable and other assets	873,387		873,387
Warrants and accounts payable	(1,384,323)		(1,384,323)
Net cash provided by operating activities	(346,272)	518,180	171,908
INCREASE / DECREASE IN CASH AND EQUIVALENTS	(346,272)	518,180	171,908
Cumulative effect of change in accounting principle (Note 15)		1,368,436	1,368,436
CASH AND EQUIVALENTS, beginning of year	<u>1,273,720</u>	<u>1,770,197</u>	<u>3,043,917</u>
CASH AND EQUIVALENTS, end of year	<u>\$927,448</u>	<u>\$3,656,813</u>	<u>\$4,584,261</u>

See notes to general purpose financial statements.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS
YEAR ENDED JUNE 30, 1998

1. Definition of Reporting Entity:

The City of Salem is governed by an elected Mayor and City Council. Generally Accepted Accounting Principles ("GAAP") require that the accompanying general purpose financial statements present the City of Salem (the primary government) and its component units. Component units are included in the City's reporting entity if their operational and financial relationships with the City are significant. Pursuant to this criteria, the following entities have been excluded from the accompanying general purpose financial statements:

- Salem Housing Authority
- South Essex Regional Sewer District
- North Shore Regional School District

The City of Salem's Retirement System (the "system") has been identified as a component unit. The system was established under the authority of Chapter 32 of the Massachusetts General Laws, as amended, and is an independent contributory retirement system available to employees of the City. The powers of the system are vested in the Retirement Board. The system has been blended into the City's Fiduciary Fund Types for reporting purposes.

2. Summary of Significant Accounting Policies:

The accounting policies of the City of Salem, Massachusetts, conform to generally accepted accounting principles as applicable to governmental units, except that the City (1) does not include a statement of general fixed assets (2) maintains its enterprise funds on a modified accrual basis of accounting which is other than the basis prescribed by generally accepted accounting principles, (3) accounts for the risk financing activities of the health claims and workmen's compensation on a basis of accounting other than generally accepted accounting principles, and (4) has not been consistent with all the required pension disclosures. The following is a summary of the more significant policies:

(a) Basis of Presentation-Fund Accounting:

The activities of the City are accounted for through the use of several funds and an account group, each of which is a separate accounting entity. The operations of each fund and account group are accounted for through a separate set of self-balancing accounts which are summarized by type in the financial statements. The following fund types and account group are used by the City.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

2. Summary of Significant Accounting Policies - continued:

(a) Basis of Presentation-Fund Accounting - continued:

Governmental Fund Types:

Government Funds are those through which most governmental functions of the City are financed. The acquisition, use and balances of the City's expendable financial resources and the related liabilities are accounted for through Governmental Funds. The measurement focus is based upon determination of changes in financial position, rather than upon net income. The following are the City's Governmental Fund types:

General Fund - The General Fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds - Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to specified purposes.

Capital Project Funds - Capital Project Funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by trust funds).

Fiduciary Fund Types:

Trust and Agency Funds - Fiduciary Funds are used to account for assets held by the City in a trustee capacity or as an agent. Trust Funds include Expendable Trust Funds and Non-expendable Trust Funds. Non-Expendable Trust Funds are reported as Proprietary Funds. Expendable Trust Funds are reported as Governmental Funds. Agency Funds are custodial in nature and do not involve measurements of results of operations.

Pension Trust Fund - The Pension Trust Fund is used to account for the assets of the City of Salem Retirement System (the System) available for the payment of retired employees' benefits and administrative expenses of the System.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

2. Summary of Significant Accounting Policies - continued:

(a) Basis of Presentation-Fund Accounting - continued:

Proprietary Fund Types:

Enterprise funds - The Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where net income and capital maintenance are measured. Costs of providing services to the general public on a continuing basis, including depreciation, are financed or recovered primarily through user charges.

Account Group:

General Long-term Obligations Account Group - This account group is used to account for all long-term obligations of the City.

(b) Measurement Focus:

All Governmental Funds and Expendable Trust Funds are accounted for on a spending or "financial flow" measurement focus. With this measurement focus, only current assets and current liabilities are generally included on the balance sheets. The reported fund balance (net current assets) is considered a measure of "available spendable resources". Governmental Fund operating statements present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Accordingly, such statements present a summary of sources and uses of "available spendable resources" during a period. Noncurrent portions of long-term receivables due to Governmental Funds are reported on their balance sheets notwithstanding their measurement focus. Special reporting treatments are used to indicate, however, that they should not be considered "available spendable resources", since they do not represent net current assets. Recognition of Governmental Fund type revenues represented by noncurrent receivables is deferred until they become current receivables.

**CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998**

2. Summary of Significant Accounting Policies - continued:

(b) Measurement Focus - continued:

Because of their spending measurement focus, expenditure recognition for Governmental Fund types is limited to exclude amounts represented by noncurrent liabilities. Since they do not affect net current assets, such long-term amounts are not recognized as Governmental Fund type expenditures or fund liabilities, but are reported as liabilities in the General Long-Term Obligations Account Group.

(c) Basis of Accounting:

The modified accrual basis of accounting is followed by Governmental Funds and Expendable Trust Funds. Under the modified accrual basis, revenue is recognized that is both measurable and available to pay liabilities of the current period. Revenues not considered available are recorded as deferred revenues. Expenditures are recorded when the liability is incurred, except for interest on general long-term obligations, which is recorded when due.

In applying the susceptible to accrual concept to intergovernmental revenues, these are essentially two types of revenues. In one, monies must be expended for the specific purpose or project before any amounts will be paid to the City; therefore, revenues are recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria are met.

Property taxes are recognized as revenue in the year for which taxes have been levied, provided they are collected within 60 days after year-end. Licenses and permits, fines and forfeitures and miscellaneous revenues are recorded as revenues when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

2. Summary of Significant Accounting Policies - continued:

(c) Basis of Accounting-continued:

The City utilizes the accrued basis of accounting with respect to expense recognition, of the Enterprise funds. The City has not maintained adequate records to properly account for other Enterprise Funds activities such as revenue recognition, the recognition of fixed assets, depreciation, and contributed capital. The above deviations as well as other modifications are necessary for the Enterprise funds to be in accordance with generally accepted accounting principles.

The accrual basis of accounting is used by trust funds.

(d) Encumbrances:

Encumbrance accounting, is employed by Governmental Funds. With encumbrance accounting purchase orders, contracts and other commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation. Open encumbrances at year-end are reported as reservations of fund balances. Encumbrances do not constitute expenditures or liabilities except for budget purposes.

(e) Investments:

Investments in bonds and stocks for the Retirement System and Trust Fund investments are carried at current fair value. Deferred compensation plan assets are invested in mutual funds, which are also carried at current fair value.

(f) Inventory:

Inventory items (materials and supplies), which are not material to the general purpose financial statements are recorded as expenditures when purchased (purchase method).

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

2. Summary of Significant Accounting Policies - continued:

(g) General Fixed Assets:

General fixed assets are recorded as expenditures in applicable Governmental Funds. The City does not capitalize the cost of general fixed assets in a General Fixed Asset Group, as is required by generally accepted accounting principles. Since the Commonwealth of Massachusetts does not require the capitalization of fixed assets, this is consistent with the practice of many municipalities in the Commonwealth of Massachusetts.

(h) Compensated Absences:

GAAP requires the accrual of a liability for vested or accumulated vacation and sick leave. Compensated absences expected to be liquidated with expendable available financial resources are reported as expenditures and fund liabilities. Accounts that are not expected to be liquidated with expendable available financial resources are reported in the General Long-Term Obligations Account Group. Employees earn vacation as they provide services. Except in certain circumstances, (i.e. pursuant to certain collective bargaining agreements), vacation time earned must be used annually and shall not be cumulative from year to year. In the case of estimated sick leave benefits only that portion of benefits calculated based on termination benefits are presented as a liability in the General Long-term Obligation Account Group at June 30, 1998.

(i) Post Retirement/Health Care and Life Insurance Benefits:

The City provides certain health care and life insurance benefits for retired employees. Substantially all of the City's employees may become eligible for those benefits if they reach normal retirement age while working for the City. Benefits paid by the City are on a pay-as-you go basis, and there is no actuarial valuation available as of June 30, 1998, which would permit an estimation of the unfunded past service cost liability, the future costs of current participants in the plan and the annual amounts needed to fund such costs.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

2. Summary of Significant Accounting Policies - continued:

(j) Deferred Compensation:

The City offers its employees a Deferred Compensation Plan created in accordance with Internal Revenue Code Section 457. The Plan, which is available to all employees, permits participants to defer a portion of their salary until future years. Amounts deferred under the Plan are not available to employees until termination, retirement, death or unforeseeable emergency.

All amounts of compensation deferred under The Plan, all property and rights purchased with the amounts, and all income attributable to these amounts are solely the property and rights of the employer, subject only to the claims of the employer's general creditors. Participants' rights under the Plan are equal to those of general creditors of the employer in an amount equal to the fair market value of the deferred account of each participant.

The City has no liability for losses under the Plan but does have the duty of due care that would be required of an ordinary prudent investor. The City believes it is unlikely that Plan assets will be used to satisfy future claims of general creditors. At June 30, 1998, assets of \$6,988,482 are recorded in the Agency Fund.

(k) Total Columns:

Total columns on the combined statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis. Data in these columns do not present financial position, results of operations or changes in financial position in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation since interfund elimination's have not been made.

(l) Comparative Data:

Summaries of comparative data, which is not required, for the prior year general fund have been presented in the accompanying general purpose financial statements to provide an understanding of changes in the general fund financial position and operations.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

3. Budgetary Accounting:

The City must establish its property tax rate each year so that the resulting property tax levy will comply with the limits required by Proposition 2-1/2 and also constitute that amount which will equal the sum of (a) the aggregate of all annual appropriations for expenditures and transfers, plus (b) a provision for the prior fiscal year's deficits, if any, less (c) the aggregate of all non-property tax revenue and transfers projected to be received by the City, including available surplus funds.

An annual budget is legally adopted for the General Fund and the Enterprise Funds. Council orders are initiated or recommended by the Mayor. Expenditures may not legally exceed appropriations at the department level. Department heads may transfer, with the Mayor's approval, appropriation balances from one expenditure account to another within their department or budget. The City Council and the Mayor must approve any transfer of unencumbered appropriation balances between departments or agencies.

At the close of each fiscal year, unencumbered appropriation balances (appropriation less expenditures and encumbrances) revert to the unreserved fund balance. Unencumbered appropriation balances in the capital project fund, however, do not lapse at the end of the fiscal year.

The budgets are prepared on a basis of accounting other than generally accepted accounting principles (GAAP). The "actual" results columns of the Statement of Revenues and Expenditures - Budget and Actual - General Fund - Budgetary Basis is presented on a "budget basis" to provide a meaningful comparison with the budget.

The major differences between the budget and GAAP basis are that:

- (a) Budgeted revenues are recorded when cash is received, except for real estate and personal property taxes, which are recorded as revenue when levied (budget), as opposed to when susceptible to accrual (GAAP).
- (b) Encumbrances and continuing appropriations are recorded as the equivalent of expenditures (budget), as opposed to a reservation of fund balances (GAAP).
- (c) Reserve fund transfers are recorded as sources (budget) as opposed to not recorded (GAAP).

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

3. Budgetary Accounting - continued:

A reconciliation of budgetary-basis to GAAP-basis results is presented below:

GAAP basis excess of revenues and other financing sources over expenditures and other financing uses	\$2,874,334
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Reconciling Items:

Transfer from unreserved fund balance	1,146,562
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Transfers recognition	399,358
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Revenue recognition	(1,608,638)
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Encumbrance/expenditure recognition	<u>406,960</u>
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Budgetary basis excess of revenues and other financing sources over expenditures and other financing uses	<u><u>\$3,218,576</u></u>
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4. Receivables - Real Estate and Personal Property:

The following schedule is a breakdown of real estate and personal property tax receivables by year:

	<u>Amount</u>
Real Estate:	
1998	\$844,011
1997 & Prior	(64,778)
Chapter 59 in Lieu of tax	<u>136,254</u>
Total Real Estate	915,487
Personal Property:	
1998	20,583
1997 & Prior	<u>6,425</u>
Total Personal Property	<u>27,008</u>
 TOTAL RECEIVABLES	 <u><u>\$942,495</u></u>

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

5. Cash and Investments:

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

In addition, the City's Fiduciary Fund types have additional investment powers, most notably the ability to invest in common stocks, corporate bonds and other specified investments.

At year end, the carrying amount of the City's deposits was \$3,769,736 and the bank balance was \$5,307,377. Of the bank balance, \$470,047 was covered by federal depository insurance, \$165,316 was covered by state depository insurance and \$4,672,014 was uninsured.

At December 31, 1997, the carrying amount deposits for the Pension Trust Fund was \$48,597 and the bank balance was \$425,567. Of the bank balance, \$100,000 was covered by federal depository insurance and \$325,567 was uninsured.

Investments are categorized into these three categories of credit risk:

- (1) Insured or registered, or securities held by the government or its agent in the government's name.
- (2) Uninsured or unregistered, with securities held by counterparty's trust department or agent in the government's name.
- (3) Uninsured or unregistered, with securities held by counterparty's trust department or agent but not in the government's name.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

5. Cash and Investments - continued:

The following schedule categorizes the City's investments:

	Category 1	Category 2	Category 3	Fair Value
The City at June 30, 1998:				
Domestic Mutual Funds	\$250,547			\$250,547
International Mutual Funds	238,978			238,978
Corporate Bonds	1,875,375			1,875,375
Stocks	2,361,101			2,361,101
	<u>4,726,001</u>			<u>4,726,001</u>
Investments not subject to categorization:				
State Treasurer's Investment Pool				3,022,639
Money markets				7,032,714
Deferred compensation plan mutual fund investment				<u>6,988,482</u>
Total City funds				21,769,836
Pension Trust Fund at December 31, 1997:				
Government obligations	854,973			854,973
Fixed income securities		\$23,371,059		23,371,059
Equity securities	28,249,312			28,249,312
	<u>29,104,285</u>	<u>23,371,059</u>		<u>52,475,344</u>
Investments not subject to categorization:				
International mutual funds				3,549,578
Real estate				<u>150,000</u>
Total Pension Trust Fund				<u>56,174,922</u>
Total				<u>\$77,944,758</u>

The following is a reconciliation of investments and cash and equivalents as summarized above to the balance as recorded in the combined balance sheet:

	Investments	Cash and Equivalents	Investments of Deferred Compensation Plan
As presented above	\$77,944,758	\$3,818,333	
Reclass: Short-term investments reported in the combined balance sheet as cash and equivalents as follows:			
Short - term government obligations	(854,973)	854,973	
Deferred compensation plan investme	(6,988,482)		6,988,482
Money market investments	(7,032,714)	7,032,714	
State Treasurer's Investment Pool	<u>(3,022,639)</u>	<u>3,022,639</u>	
Total	<u>\$60,045,950</u>	<u>\$14,728,659</u>	<u>\$6,988,482</u>

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

6. Property Taxes:

Real and personal property taxes are based on values assessed as of each January 1, and are normally due on August 1, November 1, February 1, and May 1, or thirty days subsequent to mailing date. By law, all taxable property in the Commonwealth must be assessed at 100% of fair cash value. Taxes due and unpaid after the respective due dates are subject to interest and penalties. The City has an ultimate right to foreclose on property for which taxes have not been paid. Property taxes levied are recorded as receivables, net of estimated uncollectibles, in the fiscal year of the levy. Property tax revenues are recorded in accordance with the modified accrual basis of accounting described in Note 2 (c).

A statewide tax limitation statute known as "Proposition 2 1/2" limits the property tax levy to an amount equal to 2-1/2% of the value of all taxable property in the City. A secondary limitation is that no levy in a fiscal year may exceed the preceding year's allowable tax levy by more than 2-1/2%, plus taxes levied on certain property newly added to the tax rolls. Certain Proposition 2-1/2 taxing limitations can be overridden by a City wide referendum vote.

7. Other Receivables:

The principal amounts classified as other receivables included the following at June 30, 1998:

	General Fund	Trust & Agency Fund	Pension Trust Fund	Special Revenue Fund
Motor Vehicle and Boat Excise	\$ 532,726			
Tax Liens and Foreclosures	2,342,408			
Accrued Interest			\$ 417,789	
Police Details		\$ 121,130		
Notes / Accounts Receivable			1,899,358	\$5,253,657
Payroll Taxes		97,958		
	<u>\$2,875,134</u>	<u>\$ 219,088</u>	<u>\$2,317,147</u>	<u>\$5,253,657</u>

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

7. Other Receivables - continued:

The City has retained two banks to service various term loans executed by the City as part of its business loan program for local economic development and its housing improvement program. The funding for the loans was through the United States Office of Housing and Urban Development. To date approximately 70 loans have been issued, estimating a principal amount of \$4,600,000. The remaining outstanding balance of \$2,269,010 has been reflected as a receivable in the Special Revenue Fund. The interest on these loans varies between 0% and 8% and the loans mature on various dates through 2031.

8. Note Receivable - Hospital:

The hospital's building and land were sold by the City on December 16, 1996. The negotiated purchase price was \$4.8 million after netting off undepreciated assets. Lease payments in the amount of \$316,215 were applied to the purchase price. The payment schedule to the City was made retroactive to January 1, 1996, accordingly the City received proceeds for \$1,058,003, which represents eleven monthly installments of principle, at the time of the sale. The City is to receive monthly installments of \$96,182 plus interest accruing at 7.5% until January 1, 2001. As of June 30, 1998, \$2,984,647 remained outstanding with respect to this note. This amount has been included as other receivables in the Special Revenue Fund.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

9. Bond Indebtedness:

As of June 30, 1998, the City had the following outstanding long-term debt:

	Date of Issue	Fiscal Year Of Maturity	Original Principal	Interest Rate	Amount Outstanding
<u>City Operational</u>					
<i>Inside Debt Limit:</i>					
Library	8/15/90	6/15/99	\$2,200,000	6.66%	\$ 200,000
Offstreet parking garage	7/15/91	2/15/01	1,600,000	5.0%	645,000
Police Station	1/15/94	1/15/04	200,000	5.7-8.5%	120,000
Police Station	9/1/92	1/15/12	5,450,000	4.5-7.25%	3,975,000
<i>Total inside debt limit</i>					<u>4,940,000</u>
<i>Outside Debt Limit:</i>					
Racial balance	8/15/90	6/15/00	1,500,000	6.67%	\$ 320,000
Racial balance	7/15/91	2/15/11	9,500,000	6.5-6.75%	6,500,000
Racial balance	9/1/92	1/15/12	12,000,000	5.7-8.5%	8,775,000
Racial balance	1/15/94	1/15/13	9,000,000	4.6-7.25%	7,100,000
School	8/15/90	6/15/00	900,000	6.66%	200,000
School	7/1/96	8/15/15	7,000,000	5.48%	6,810,000
School	7/1/96	8/15/15	1,800,000	5.48%	1,700,000
<i>Total outside debt limit</i>					<u>31,405,000</u>
Total City Operational					
<u>Enterprise</u>					
<i>Outside Debt Limit:</i>					
Water supply	8/15/90	6/15/00	1,175,000	6.66%	\$ 155,000
Water supply	7/15/91	2/15/02	690,000	6.36%	270,000
Water supply	1/15/94	1/15/04	1,050,000	4.56%	630,000
Total Enterprise					<u>1,055,000</u>
<u>Community Development</u>					
<i>Outside Debt Limit:</i>					
HUD 108 1995-A	2/1/95	8/1/14	600,000	9.0%	\$ 570,000
HUD 108 1989-A	6/29/89	8/1/99	600,000	4.38%	600,000
Total Community Development					<u>1,170,000</u>
TOTAL DEBT					<u><u>\$38,570,000</u></u>

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

9. Bond Indebtedness - continued:

The following summarizes long-term debt transactions of the City for the year ended June 30, 1998:

Bonds payable at July 1, 1997	\$41,950,000
Additions	
Retirements	<u>(3,380,000)</u>
Bonds payable at June 30, 1998	<u>\$38,570,000</u>

Payments on general long term obligation bonds due in future years consist of the following for the year ending June 30:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
1999	\$ 3,295,000	\$ 2,121,077	\$ 5,416,077
2000	3,595,000	1,911,151	5,506,151
2001	2,735,000	1,721,425	4,456,425
2002	2,520,000	1,581,916	4,101,916
2003	2,445,000	1,447,956	3,892,956
Thereafter	<u>23,980,000</u>	<u>6,924,364</u>	<u>30,904,364</u>
	<u>\$38,570,000</u>	<u>\$15,707,889</u>	<u>\$54,277,889</u>

At June 30, 1998, the City has authorized and unissued debt of \$100,000.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

9. Bond Indebtedness - continued:

(a) Legal Debt Margin

The City is subject to the General Laws of the Commonwealth of Massachusetts which limits the amount of bonded debt (exclusive of several categories of general obligation debt issues exempt from the debt limit) the City may have outstanding up to 2 ½% of the valuation of taxable property as last equalized by the Commonwealth's Department of Revenue. The following is a computation of the legal debt margin as of June 30, 1998 (in thousands of dollars):

Equalized Valuation - Real Estate and Personal Property		\$2,063,726
Debt Limit - 2 ½% of Equalized Valuation		51,593
Total Debt	\$38,570	
Less: Debt Exempt from Limit	(34,075)	<u>(4,495)</u>
Legal Debt Margin		<u>\$ 47,098</u>

(b) Overlapping Debt:

The City's proportionate share of debt of other governmental units which provide services within the City's boundaries, and which is annually assessed to the City, is summarized below (unaudited):

<u>Related Entity</u>	<u>Principal (thousands)</u>	<u>Percent</u>	<u>Amount</u>
Essex County	\$ 850	5.90%	\$ 50,150
MBTA	2,399,780	.69%	16,558,482
South Essex Sewer District	207,942	25.49%	<u>53,004,473</u>
			<u>\$69,613,105</u>

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

10. Temporary Borrowing:

The City is authorized to borrow on a temporary basis to fund the following:

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

Temporary loans are general obligations of the City and carry maturity dates which are limited by statute. Interest expenditures for temporary borrowing are accounted for in the general fund. The City has a Capital Projects Fund BAN totaling \$400,160 bearing an interest rate of 3.85% and maturing December 16, 1998.

11. Contingencies:

Various legal actions and claims are pending against the City. Litigation is subject to many uncertainties, and the outcome of individual litigated matters is not always predictable. Although the amount of liability, if any, at June 30, 1998, cannot be ascertained, management believes any resulting liability should not materially affect the financial position of the City at June 30, 1998.

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

The City is subject to certain federal arbitrage laws in accordance with its long-term borrowings. Failure to comply with the rules could result in the payment of penalties. The amount of penalties, if any, cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

11. Contingencies - continued:

In March 1993, the City was awarded approximately \$1,800,000 in damages as a result of a lawsuit against the Commonwealth of Massachusetts. The state has filed an appeal, and no judgment has been rendered by the Appeals Court. Accordingly, this judgment has not been recognized in the City's general purpose financial statements.

The Year 2000 problem affects the City's computer systems and other equipment necessary for its continued and uninterrupted operations. The City is in the implementation stage of work necessary to make its systems Year 2000 compliant. The City intends on replacing all computing platforms, hardware and software prior to the year 2000, therefore with these upgrades all systems will be compliant by December 31, 1999. The estimated cost of this replacement is \$700,000.

12. Retirement System:

Plan Description:

The City contributes to the City of Salem Contributory Retirement System (the Plan), a multiple employer defined benefit pension plan, established under Chapter 32 of the General Laws of the Commonwealth of Massachusetts. The Plan is administered by the City of Salem and is part of the reporting entity. A stand alone annual statement was issued for the year ended December 31, 1997. This report is available at the Retirement Office, 93 Washington Street, Salem, Massachusetts.

Substantially all full-time employees of the City, except teachers and certain administrative personnel employed by the School Department, participate in the Plan. The members of the retirement system do not participate in the Social Security System. Benefits paid under the Plan, referred to as "retirement allowances," include both an annuity portion, funded principally from amounts contributed by the participants, and a pension portion, funded by the City. The City's payroll for employees covered by the Plan for the year ended December 31, 1997, was approximately \$18,800,000.

Teachers and certain administrative employees of the School Department participate in a contributory retirement plan administered by the Massachusetts Teachers Retirement Board. Contributions to the Plan are made entirely by the Commonwealth of Massachusetts, and therefore, the City does not contribute to this plan.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

12. Retirement System - continued:

Membership:

Current membership in the Plan as of January 1, 1998, is as follows:

Retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them	658
Active employees	<u>520</u>
Total	<u><u>1,178</u></u>

Benefits:

Massachusetts Contributory Retirement System benefits are uniform from system to system. The System provides for retirement allowance benefits up to a maximum of 80% of a participant's highest three-year average annual rate of regular compensation. Benefit payments are based upon a participant's age, length of creditable service, level of compensation and group classification.

The retirement allowance consists of two parts: an annuity and a pension. Participants' accumulated total deductions and a portion of the interest they generate constitute the annuity. The differential between the total retirement benefit and annuity is the pension.

In previous years, the Legislature granted cost-of-living increases to benefits being paid to retirees. These increases were expressed as a percentage of the retiree's allowance subject to a maximum dollar increase. Since 1982, cost-of-living increases granted to members of local retirement systems have been the financial responsibility of the State. However, beginning in 1998, the funding of future cost-of-living amounts became the responsibility of the individual communities. These communities are responsible for the full amounts for all new retirees beginning that year, and for any additional cost-of-living increases granted to individuals who retired before 1998. The State shall continue to fund the cost-of-living amounts previously granted to those who received support under the old method, but only for the duration of the retirees' selected, retirement option.

Participants who resign from service and who are not eligible to receive a retirement allowance or are under the age of 55 are entitled to request a refund of their accumulated total contributions. In addition, depending upon the number of years of creditable service, such employees are entitled to receive either 0%, 50% or 100% of the regular interest which has accrued upon those contributions. A vested employee under the age of 55 who elects to leave his accumulation on deposit may apply for benefits upon reaching that age.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

12. Retirement System - continued:

Benefits - continued:

Survivor benefits are extended to eligible beneficiaries of participants whose death occurs prior to or following retirement.

The System may be amended or terminated in whole or in part at any time by the Massachusetts Legislature, provided that no such modification, amendment or termination shall be made that would deprive a current member of superannuation pension rights or benefits provided under applicable laws of Massachusetts, if such member has paid the stipulated contributions specified in sections or provisions of such laws.

Normal Retirement:

Normal retirement occurs at age 65; however, participants may retire after twenty years of service or at any time after attaining age 55. Participants with hire dates subsequent to January 1, 1978, must have minimum of ten years' creditable service in order to retire at age 55. Participants become vested after ten years of service. Benefits commencing before age 65 are provided at a reduced rate. Members working in certain occupations may retire with full benefits earlier than age 65.

Disability Retirement:

The System provides for both an ordinary disability retirement, where a participant is permanently incapacitated from a cause unrelated to employment, and an accidental disability retirement, where the disability is the result of an injury or illness received or aggravated in the performance of duty. The amount of benefits to be received in such cases is dependent upon several factors, including the age at which the disability retirement occurs, the years of service, average compensation and veteran status.

Funding Status and Progress:

The City has elected provisions of Chapter 32, Section 22D of Massachusetts General Laws, which require that a funding schedule be established to fully fund the accrued liability by June 30, 2021. Under provisions of this law, participating employers are assessed their share of the total retirement cost based on the entry age, normal actuarial cost method. Amortization of the unfunded actuarial liability is determined using the level dollar amortization method over a 27-year period.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

12. Retirement System - continued:

Contribution Requirements and Contributions Made:

The Plan's funding policies have been established by Chapter 32 of the Massachusetts General Laws. The annuity portion of the retirement allowance is funded by employees who contribute a percentage of their regular compensation. Employees whose creditable service began prior to January 1, 1975, contribute 5% of their base salary or wage; those whose service date is subsequent to January 1, 1975, and prior to January 1, 1984, contribute 7%; those whose service date is subsequent to January 1, 1984, and prior to July 1, 1996, contribute 8%, and those whose service date is subsequent to July 1, 1996, contribute 9%. Additionally, employees hired after January 1979 contribute an additional 2% on earnings in excess of \$30,000.

In accordance with Massachusetts General Laws, employer contributions to the Plan have historically been determined on a pay-as-you-go basis. GAAP requires that the annual minimum provision for pension costs should include normal cost, interest on unfunded past service cost liability, and amortization of unfunded vested benefits, based on an acceptable actuarial cost method.

The Pension Reform Act of 1987 was enacted by the State Legislature in January 1988. The Act amends Chapter 32 of the General Laws and requires amortization of the unfunded pension liability over a forty-year period.

The employer contribution to the Plan for the year ended December 31, 1997, 1996, and 1995 was \$3,211,000, \$3,221,000 and \$4,052,000 respectively, which equaled its required contribution for each year.

GAAP requires disclosure of the actuarial value of plan assets, the actuarial accrued liability, the annual required contribution and the determination of the net pension obligation or asset which would require inclusion in the General Long-Term Obligations Account Group. The City has not had an acceptable actuarial valuation performed to determine these amounts accordingly this required supplementary information has not been disclosed.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

13. Risk Financing:

The City has established a self-insured medical program which is accounted for in the Health Claims Trust Fund, an expendable trust fund. Both employees and the City contribute to the payment of medical claims based upon primary care premium formula. The percentage is dependent upon the plan that is selected. The employee portion is paid into the Health Claims Trust Fund. The City's portion is appropriated in the general fund and transferred out to be expended from the expendable trust fund. The purpose of this program is to pay medical claims of the City's employees and their covered dependents. The City carries insurance on individual medical claims in excess of \$100,000 annually. Estimated losses on claims are charged to expenditures in the period the claim is determinable. The City accrues claims submitted for medical services rendered prior to June 30, 1998.

The City has also established self-insurance programs for unemployment and workers' compensation claims. Workers' compensation claims are appropriated for as part of the annual budget. Unemployment claims are paid to employees by the Commonwealth of Massachusetts, for which the City is billed on a monthly basis.

The City engages an independent insurance carrier for all casualty insurance.

The above is not in accordance with generally accepted accounting principles which require that such activities be recorded either in the general fund or in an internal service fund. Additionally, generally accepted accounting principles require that an actuarial valuation be determined for claims incurred but not reported, and that this amount be accrued in the general long-term obligations group of accounts.

14. Fund Deficits:

The City incurred a deficit of \$68,989 on state and county assessments and debt payments of \$6,378. This is anticipated to be raised on future tax recapitulation sheets.

15. Change in Accounting Principle:

During 1998, the City adopted the requirements of Governmental Accounting Standards Board's Statements No. 25 and 31, which resulted in adjustments to increase the beginning plan net assets of the System by \$18,554 and the beginning fund balances of the Nonexpendable Trust Funds by \$1,368,436. These adjustments were necessary to reflect the changes in valuation of investments to fair value.

CITY OF SALEM, MASSACHUSETTS
NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - CONTINUED
YEAR ENDED JUNE 30, 1998

16. Stabilization:

In accordance with Massachusetts General Laws, the City has established a stabilization fund to be utilized as an additional reserve fund. The fund is subject to appropriation at the discretion of the Emergency Finance Board and a two-thirds vote of the City Council. The activities of this fund, which had a balance of approximately \$639,005 as of June 30, 1998, is accounted for as an Expendable Trust Fund.

17. Segment Information for Enterprise Funds:

The City maintains Enterprise funds which provide water and sewer services. Segment information for the year ended June 30, 1998 follows:

	<u>Water</u>	<u>Sewer</u>	<u>Total</u>
Revenues	\$2,872,212	\$5,768,957	\$8,641,169
Expenses	(1,463,041)	(5,996,056)	(7,459,097)
Debt Expense:			
Principal	(330,000)		(330,000)
Interest	(70,618)		(70,618)
Transfer(s) In	17,166		17,166
Indirect Costs Paid to the General Fund	<u>(316,978)</u>	<u>(316,978)</u>	<u>(633,956)</u>
Net Income (Deficit)	708,741	(544,077)	164,664
Retained Earnings July 1, 1997	<u>761,165</u>	<u>475,832</u>	<u>1,236,997</u>
Retained Earnings June 30, 1998	<u>\$ 1,469,906</u>	<u>\$ (68,245)</u>	<u>\$ 1,401,661</u>

**CITY OF SALEM, MASSACHUSETTS
RECONCILIATION OF TREASURER'S CASH
YEAR ENDED JUNE 30, 1998**

Treasurer's cash and equivalents balance, June 30, 1998	<u>\$14,728,659</u>
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Composition of balance on June 30, 1998:

State Street Bank and Trust Company	456,608
BankBoston	893,827
Boston Safe Company	5,127,356
Eastern Bank	3,761,706
Salem Five Cents Savings Bank	365,727
Century Bank and Trust	157,408
Fleet Bank	1,577,292
Greater Salem Employees Federal Credit Union	167
Pension Trust Fund (as of December 31, 1997)	1,280,540
Massachusetts Municipal Depository Trust	<u>3,022,639</u>
	<u>\$16,643,270</u>

Reconciling Items:

Outstanding checks	(2,938,092)
Deposits in transit	1,133,399
Other	<u>(109,918)</u>
	<u>\$14,728,659</u>

Presentation of cash and equivalents
in balance sheet on June 30, 1998:

General Fund	\$9,404,931
Special Revenue Fund	693,153
Capital Projects Fund	36,679
Trust and Agency Funds	2,762,878
Enterprise fund	927,448
Pension Trust Fund (as of December 31, 1997)	<u>903,570</u>
	<u>\$14,728,659</u>

**CITY OF SALEM, MASSACHUSETTS
REQUIRED SUPPLEMENTARY INFORMATION
STATEMENT OF PLAN NET ASSETS
DECEMBER 31, 1997**

ASSETS

INVESTMENTS (at fair value):

Bonds	\$23,371,059
Stocks	28,249,312
Equity mutual funds	3,549,578
Limited partnerships	<u>150,000</u>

Total Investments	<u>55,319,949</u>
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CASH AND CASH EQUIVALENTS	<u>903,570</u>
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RECEIVABLES:

Accounts receivable	1,899,358
Interest due and accrued	<u>417,789</u>

Total Receivables	<u>2,317,147</u>
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Total Assets	<u><u>58,540,666</u></u>
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<u>NET ASSETS HELD IN TRUST FOR PENSION BENEFITS</u>	<u><u>\$58,540,666</u></u>
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**CITY OF SALEM, MASSACHUSETTS
REQUIRED SUPPLEMENTARY INFORMATION
STATEMENT OF CHANGES IN PLAN NET ASSETS
YEAR ENDED DECEMBER 31, 1997**

ADDITIONS

Contributions:	
Employer	\$4,344,888
Employee	1,830,230
From Commonwealth of Massachusetts	748,052
From other systems and miscellaneous	207,224
Investment Income	594,268
Net gain on investments (including realized and unrealized gains and losses)	<u>8,003,817</u>
 Total Additions	 <u>15,728,479</u>

DEDUCTIONS

Benefit payments to retirees, survivors and disability retirees	7,442,158
Refunds to members leaving the System	389,409
Transfers to other systems	260,672
Payroll expenses of the System	93,558
Other administrative expenses	<u>302,843</u>
 Total Deductions	 <u>8,488,640</u>

INCREASE IN NET ASSETS	<u>7,239,839</u>
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NET ASSETS HELD IN TRUST FOR PENSION BENEFITS

Beginning of year	\$51,282,273
Cumulative effect of change in accounting principle (Note 15)	<u>18,554</u>
End of year	<u><u>\$58,540,666</u></u>