

**CITY OF SALEM, MASSACHUSETTS**

Report on Examination of  
Basic Financial Statements  
and Additional Information  
Year Ended June 30, 2002

**CITY OF SALEM, MASSACHUSETTS**

**TABLE OF CONTENTS**  
**YEAR ENDED JUNE 30, 2002**

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	<u>Page</u>
<u>INDEPENDENT AUDITORS' REPORT</u>	1
<u>MANAGEMENT'S DISCUSSION AND ANALYSIS</u>	2-12
<u>BASIC FINANCIAL STATEMENTS:</u>	
Government-Wide Financial Statements:	
Statement of Net Assets	13
Statement of Activities	14
Fund Financial Statements:	
Balance sheet – Governmental Funds	15
Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds	16
Reconciliations:	
Governmental Funds Balance Sheet Total Fund Balances to the Statement of Net Assets	17
Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities	18
Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual – General Fund	19
Statement of Net Assets – Proprietary Funds	20
Statement of Revenues, Expenses, and Changes in Fund Net Assets – Proprietary Funds	21
Statement of Cash Flows – Proprietary Funds	22
Statement of Fiduciary Net Assets	23
Statement of Changes in Fiduciary Net Assets	24
Notes to Basic Financial Statements	25-46
<u>REQUIRED SUPPLEMENTARY INFORMATION:</u>	
Retirement System:	
Schedule of Funding Progress	47
Schedule of Contribution from Employees	47
Other Required Supplemental Pension Disclosures	47

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# TUCCI & ROSELLI

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CERTIFIED PUBLIC ACCOUNTANTS  
MANAGEMENT CONSULTANTS

## INDEPENDENT AUDITORS' REPORT

The Honorable Mayor and Members of the City Council  
City of Salem, Massachusetts

We have audited the accompanying basic financial statements of the City of Salem, Massachusetts, as listed in the table of contents, as of and for the year ended June 30, 2002, (except for the Pension Trust Fund which is as of December 31, 2001). These basic financial statements are the responsibility of the management of the City of Salem, Massachusetts. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as, evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based upon our audit, such basic financial statements present fairly, the financial position of the City of Salem, Massachusetts, as of June 30, 2002, (except for the Pension Trust Fund which is as of December 31, 2001) and the results of its operations and the cash flows of its Proprietary Fund types for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The additional financial information listed as Management's Discussion and Analysis and required supplementary information in the table of contents is a required part of the basic financial statements of the City of Salem, Massachusetts. This additional information is the responsibility of the City's management. Such additional information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, based on our audit, is fairly presented in all material respects when considered in relation to the financial statements of each of the individual funds taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated December 5, 2002 on our consideration of the City of Salem's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

*Tucci & Roselli*

Tucci & Roselli  
Certified Public Accountants  
December 5, 2002

## Management's Discussion and Analysis

As the management of the City of Salem, Massachusetts (the City), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2002. We encourage readers to consider the information presented here in conjunction with their review of the basic financial statements and notes to the basic financial statements found on pages 13 – 46 and the required supplementary information found on page 47. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

### Financial Highlights

- The assets of the City exceeded its liabilities at the close of the most recent fiscal year by \$76.5 million (*total net assets*). Of this amount, \$13.5 million (*total unrestricted net assets*) may be used to meet the government's ongoing obligations to citizens and creditors.
- The City has not capitalized infrastructure capital assets. This will be provided in future years as the information becomes available.
- The government's total net assets experienced a net increase of \$11.6 million that is mainly attributable to three items. (1) Additions approximating \$19 million to the City's receivable balances during the year that relate to reimbursements under the School Business Assistance Reimbursement under Chapter 645 of the Acts of 1948 from the Commonwealth of Massachusetts "the Commonwealth" were recorded and resulted in an increase to net assets. (2) Approximately \$2.6 million of this is attributable to depreciation, which the City does not fund from revenue sources and resulted in a decrease to net assets. (3) Approximately \$4.8 million is attributable to one-time expenses that the City chose to fund from available beginning unrestricted equity balances that also resulted in a decrease to net assets.
- As of the close of the current fiscal year, the City's governmental funds balance sheet reported a combined ending fund deficit of \$7.8 million a decrease of \$10.9 million. This included a deficit in Capital projects funds of \$26.7 million attributable to expenditures associated with ongoing capital projects that the City expects to fund at a future date through bond issuances. These expenditures are currently financed with bond anticipation notes. The combined ending fund balance without regard to this deficit was \$18.9 million. Of the overall decrease, \$10.1 million was a direct result of the expenditures associated with the ongoing Capital projects, and the remaining \$0.7 million attributable to one-time expenditures that the City chose to fund from available beginning fund balances. \$6.9 million of the ending fund balance is *available for spending* at the government's discretion either as *unreserved fund balance* or *stabilization*. The remainder is earmarked for specific expenditures.
- The accounting treatment for certain items vary greatly between the Statement of Net Assets and the Governmental Fund Balance sheet thus the significant differences in equity and fund balance amounts between the two statements noted above. A reconciliation has been provided on page 21 of the accompanying basic financial statements to assist the reader to understand these differences.
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$4.6 million, or 5.1% percent of total general fund expenditures.
- The City's total debt decreased by \$2.8 million during the current fiscal year due to principal payments of debt. The City's short-term obligations which it expects to refinance as long-term bonds increased by \$7.7 million.

## Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves. The City adopted the provisions of Governmental Accounting Standards Board Statement No. 34 – Basic Financial Statements – Management Discussion and Analysis for State and Local Governments (GASB 34) effective June 30, 2002. The City made the decision to early implement this standard since the requirements of GASB 34 were not mandatory for the City until June 30, 2003.

**Government-wide financial statements.** The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

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

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

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

The government-wide financial statements can be found on pages 13-14 of this report.

**Fund financial statements.** A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City 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. Reconciliations are provided on pages 17-18 to facilitate this comparison between *governmental funds* and *governmental activities*.

The City maintains five individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund and the stabilization fund, both of which are considered to be major funds. Data from the other three governmental funds are combined into a single, aggregated presentation.

The City adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget on page 19.

The basic governmental fund financial statements can be found on pages 15-16 of this report.

**Proprietary funds.** The City maintains one type of proprietary fund. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses enterprise funds to account for its water and sewer enterprise, parking activities and golf course.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the water and sewer enterprise, parking activities and for the golf course. The basic proprietary fund financial statements can be found on pages 20-22 of this report.

**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 statement 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.

The basic fiduciary fund financial statements can be found of pages 23-24 of this report.

**Notes to the financial statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found of pages 25-46 of this report.

**Other information.** In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension benefits to its employees. Required supplementary information can be found on page 47 of this report.

## Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$76.5 million at the close of the most recent fiscal year.

Net Assets						
	Governmental activities		Business - type activities		Total	
	2002	2001	2002	2001	2002	2001
<b>Assets</b>						
Current and other assets	\$ 86,141	\$ 73,866	\$ 5,854	\$ 8,381	\$ 91,995	\$ 82,247
Capital assets	67,493	60,164	5,932	6,154	73,425	66,318
Total assets	153,634	134,030	11,786	14,535	165,420	148,565
<b>Liabilities</b>						
Long-term liabilities outstanding	61,053	43,208	515	650	61,568	43,858
Other liabilities	26,953	39,444	382	329	27,335	39,773
Total liabilities	88,006	82,652	897	979	88,903	83,631
<b>Net Assets</b>						
Invested in capital assets, net of related debt	55,159	51,664	5,282	5,304	60,441	56,968
Restricted	192	(11,445)	2,397	2,688	2,589	(8,757)
Unrestricted	10,276	11,159	3,210	5,564	13,486	16,723
Total net assets	\$ 65,627	\$ 51,378	\$ 10,889	\$ 13,556	\$ 76,516	\$ 64,934

By far the largest portion (79%) of the City's net assets reflects its investment in capital assets (e.g. land, buildings, machinery, and equipment), less any related debt (netted down by those amounts expected to be reimbursed by the Commonwealth) used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its 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 the City's net assets (3.4%) represents resources that are subject to external restriction on how they may be used. The remaining balance of *unrestricted net assets*, \$13.5 million, may be used to meet the government's ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the City is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities. In the prior year, restricted net assets was presented as a deficit that was attributable to expenses associated with on going capital projects which were financed through short-term borrowings that were reflected as long-term in the current year, because they were refinanced to long-term bonds subsequent to the balance sheet date. Restricted net assets reported in connection with the City's business-type activities were consistent in amount from year to year. These restricted net assets represent equity that the City maintains in its joint venture sewage activity.

The government's total net assets experienced a net increase of \$11.5 million that is mainly attributable to three items. (1) Additions approximating \$19 million to the City's receivable balances during the year that relate to reimbursements under the School Business Assistance Reimbursement under Chapter 645 of the Acts of 1948 from the Commonwealth were recorded and resulted in an increase to net assets. (2) Approximately \$2.6 million of is attributable to depreciation, which the City does not fund from revenue sources and resulted in a decrease to net assets. (3) Approximately \$4.8 million is attributable to one-time expenses that the City chose to fund from available beginning unrestricted equity balances that also resulted in a decrease to net assets.

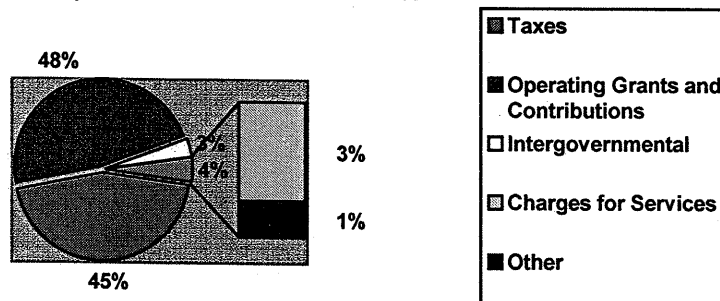
**Governmental activities.** Governmental activities increased the City's net assets by \$14.3. This net increase was made up of increases and decreases whose net effect accounted for most of the total growth in the net assets of the City. Major revenue sources consist of revenue from Operating Grants, which comprise a form of Intergovernmental revenues and represent 48% of the total revenues of the City. Additionally, the City relies on 44% of its revenues to come from property taxes.

	Changes in Net Assets					
	Governmental activities		Business - type activities		Total	
	2002	2001	2002	2001	2002	2001
<b>Revenues</b>						
Program revenues:						
Charges for services	\$ 4,029	\$ 4,242	\$ 11,682	\$ 11,989	\$ 15,711	\$ 16,231
Operating grants and contributions	57,327	42,227			57,327	42,227
Capital grants and contributions	858	434			858	434
General revenues:						
Property taxes	49,487	48,119			49,487	48,119
Other taxes	3,626	3,684			3,626	3,684
Other	4,890	11,230			4,890	11,230
Total revenues	120,217	109,936	11,682	11,989	131,899	121,925
<b>Expenses</b>						
General government	4,847	5,303			4,847	5,303
Public safety	15,493	14,865			15,493	14,865
Education	48,560	46,369			48,560	46,369
Public works	4,430	5,692			4,430	5,692
Health and human services	1,068	1,023			1,068	1,023
Culture and recreation	2,710	3,211			2,710	3,211
Pension benefits	8,506	8,492			8,506	8,492
Fringe benefits	9,955	8,137			9,955	8,137
State and County charges	3,771	2,183			3,771	2,183
Debt service	3,047	2,597			3,047	2,597
Community development	5,856	1,813			5,856	1,813
Water and sewer			10,967	8,681	10,967	8,681
Parking			719	692	719	692
Golf			388	350	388	350
Total expenses	108,243	99,685	12,074	9,723	120,317	109,408
Increase in net assets before transfers	11,974	10,251	(392)	2,266	11,582	12,517
Transfers	2,275	1,274	(2,275)	(1,274)		
Increase in net assets	14,249	11,525	(2,667)	992	11,582	12,517
Net assets, beginning of year	51,378	39,853	13,556	12,563	64,934	52,416
Net assets, end of year	\$ 65,627	\$ 51,378	\$ 10,889	\$ 13,555	\$ 76,516	\$ 64,933

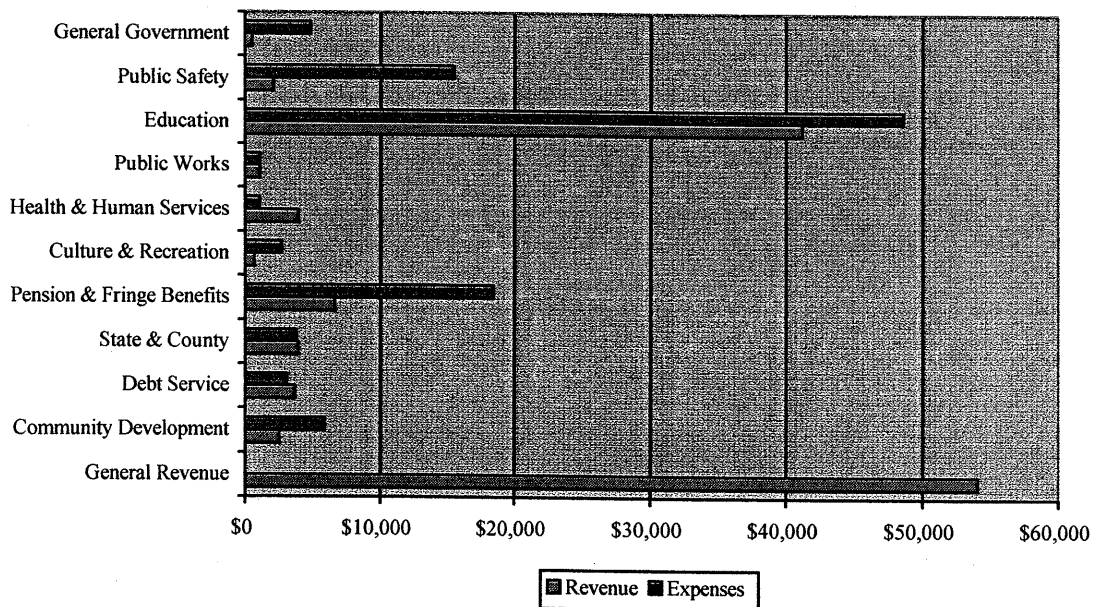


- Operating grants for governmental activities increased by \$15.1 million (35.8%), mostly as a result of additional reimbursements granted under Chapter 645 School building Assistance for new bond issuances.
- Depreciation expense is not factored into the City's budgetary process accordingly the calculated expense amount will always have a negative impact on net assets. Net assets were decreased by \$2.3 million for depreciation expense during the year.
- The City incurred some one-time charges, most notably in Community development. The increase of \$4 million decreased net assets.
- Other increases in expenses and revenues for the most part closely paralleled inflation and the growth in demand for services.

**Revenues by Source - Governmental Activities**

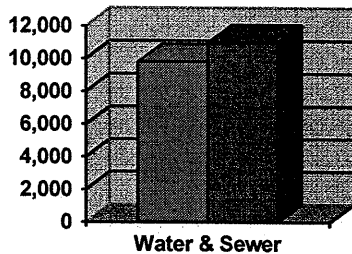


**Expenses and Program Revenues - Governmental Activities**

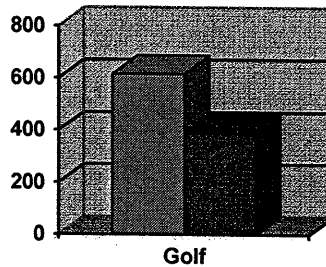


**Business-type activities.** Business-type activities decreased the City's net assets by \$2.7 million. The key element of this decrease is the following:

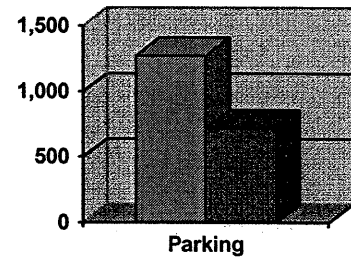
- One-time maintenance items that were financed from available beginning equity balances reduced net assets by approximately \$1.9 million.
- User charges for the water and sewer activities were \$1.1 million less than the previous year. Despite being offset by an increase in parking revenue \$0.3 million, the overall decline reduced net assets by \$0.8 million.



■ Revenue ■ Expense



■ Revenue ■ Expense



■ Revenue ■ Expense

### Financial Analysis of the Government's Funds

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

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

#### Summary information

Governmental funds			Proprietary funds			Fiduciary funds		
	2002	2001		2002	2001		2002	2001
Assets	\$ 67,109	\$ 73,866	Assets	\$ 11,786	\$ 14,535	Assets	\$ 72,212	\$ 75,327
Liabilities	74,885	70,771	Liabilities	896,706	979	Liabilities	130	110
Fund balances	\$ (7,776)	\$ 3,095	Net assets	\$ 10,889	\$ 13,556	Net assets	\$ 72,082	\$ 75,217

Governmental funds			Proprietary funds			Fiduciary funds		
	2002	2001		2002	2001		2002	2001
Revenues	\$ 105,810	\$ 116,814	Revenues	\$ 11,682	\$ 12,460	Additions	\$ 6,395	\$ 10,160
Expenditures	118,956	119,485	Expenses	12,074	11,426	Expenditures	9,529	9,255
Transfers	2,275	1,273	Transfers	(2,275)	(1,273)	Transfers		

The City's governmental funds balance sheet reported a combined ending fund deficit of \$7.8 million a decrease of \$10.8 million. This included a deficit in Capital projects funds of \$26.7 million attributable to expenditures associated with ongoing capital projects that the City expects to fund at a future date through bond issuances. These expenditures are currently financed with bond anticipation notes. The combined ending fund balance without regard to this deficit was \$18.9 million. Of the overall decrease, \$10.1 million was a direct result of the expenditures associated with the ongoing Capital projects, and the remaining \$0.7 million attributable to one-time expenditures that the City chose to fund from available beginning fund balances. \$6.9 million of the ending fund balance is *available for spending* at the government's discretion either as *unreserved fund balance* or *stabilization*. The remainder of fund balance is *reserved* to indicate that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior period \$1.4 million, 2) to generate income to pay for the perpetual care of the municipal cemetery and other trust activities \$4.6 million, or 3) for a variety of other restricted purposes \$6 million.

The general fund is the chief operating fund of the City. At the end of the current fiscal year, unreserved fund balance of the general fund was \$4.6 million, while total fund balance reached \$6.1 million. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 5.1 percent of total general fund expenditures, while total fund balance represents 6.7 percent of that same amount.

The fund balance of the City's general fund decreased by \$1.3 million during the current fiscal year mostly as a result of:

- One-time charges funded from beginning available fund balances

The stabilization fund has a total fund balance of \$2.2 million. These are unencumbered accumulated financial resources that are subject to appropriation as directed by the City's legislative branch. These funds are typically used for nonrecurring expenditures, usually capital in nature or unexpected items that may arise during the year. The net increase in fund balance during the current year was as a result of transfers from available beginning general fund balances in the amount of \$0.5 million.

**Proprietary funds.** The City's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net assets of the water and sewer fund at the end of the year amounted to \$5.3 million those for the golf course operation amounted to \$0.5 million and those of the parking program amounted to \$5.1 million. The total change in net assets for these funds have already been addressed in the discussion of the City's business-type activities.

### **General Fund Budgetary Highlights**

Differences between the original budget and the final amended budget were relatively minor (1.9 % increase in appropriation) and can be briefly summarized as follows:

- \$0.4 million in miscellaneous increases in general government activities
- \$0.7 million increases allocated to the public safety
- \$0.3 million increases allocated to the education
- \$0.3 million increases allocated to other various departments

All of this increase \$1.6 million was budgeted from available fund balance.

## Capital Asset and Debt Administration

**Capital Assets.** The City's investment in capital assets for its governmental and business type activities as of June 30, 2002, amounts to \$73.4 million (net of accumulated depreciation). This investment in capital assets includes land, buildings and system, improvements, machinery and equipment (The City has elected not to present infrastructure information until the mandated deadline in 2007). The total increase in the City's investment in capital assets for the current fiscal year was 10.7 percent (a 10.9 percent increase for governmental activities and a 3.7 percent decrease for business-type activities).

Capital Assets						
	Governmental activities		Business - type activities		Total	
	2002	2001	2002	2001	2002	2001
Land	\$ 4,684	\$ 4,684	\$ 276	\$ 276	\$ 4,960	\$ 4,960
Buildings and improvements	73,113	68,499	8,084	8,084	81,197	76,583
Improvements other than buildings	2,002	1,550	438	438	2,440	1,988
Construction in process	5,963	1,895			5,963	1,895
Machinery and equipment	2,997	2,812	219	219	3,216	3,031
Vehicles	6,043	5,688	136	136	6,179	5,824
	94,802	85,128	9,153	9,153	103,955	94,281
Less: Accumulated depreciation	(27,309)	(24,964)	(3,000)	(3,221)	(30,309)	(28,185)
Total capital assets	\$ 67,493	\$ 60,164	\$ 6,153	\$ 5,932	\$ 73,646	\$ 66,096

The City is undergoing major renovations and building of its educational facilities. Final costs will approximate \$100 million. Under Chapter 645 (School Building Assistance Reimbursement) of the Massachusetts General Laws the City is allowed to recoup a percentage of the construction costs including interest over the period of time in which the City is to pay back bonds undertaken for the various projects. The City has qualified to receive 90% reimbursements for such costs.

Additional information on the City capital assets can be found in note III. D on pages 35-36 of this report.

**Long-term debt.** At the end of the current fiscal year, the City had total debt outstanding of \$60.3 million. The entire amount comprises debt backed by the full faith and credit of the government.

Outstanding debt						
	Governmental activities		Business - type activities		Total	
	2002	2001	2002	2001	2002	2001
General obligation bonds	\$ 37,625	\$ 40,230	\$ 650	\$ 850	\$ 38,275	\$ 41,080
Notes payable	880	965			880	965
Bond anticipation notes refinanced as long term subsequent to balance sheet date	21,146				21,146	
Total debt	\$ 59,651	\$ 41,195	\$ 650	\$ 850	\$ 60,301	\$ 42,045

The City's total debt increased by \$18.3 million (43.4 percent) during the current fiscal year. The key factor in this increase was a \$28.7 million bond issuance subsequent to the balance sheet date of which \$21.1 million related to debt maintained on a short-term basis as of year-end. The City has taken the position that since this debt was refinanced prior to the issuance of the basic financial statements then it is permitted to characterize this debt as long-term on the June 30, 2002 balance sheet.

During the current fiscal year, the government refinanced some of its existing debt to take advantage of favorable interest rates. This is expected to decrease future debt service payments by approximately \$1 million.

The City maintains an "A+" rating from Standard & Poor and an "A1" rating from Moodys for general obligation debt.

State statutes limit the amount of general obligation debt a governmental entity may issue to 2.5% percent of its total assessed valuation. The current debt limitation for the City is \$2.9 billion, which is significantly in excess of the City's outstanding general obligation debt.

The City also holds a proportionate share of debt of other governmental units that provide services within the City's boundaries. The debt service from such arrangements is assessed annually to the City. Total amount of such overlapping debt approximates \$66.7 million.

The City has also entered into various lease agreements and minor notes payable agreements in the total amount of \$2 million.

Bond anticipation notes payable balances outstanding at year-end, that have not been converted to long-term amount to \$14.5 million and all relate to school construction projects.

Additional information on the City's long-term debt can be found in note III.F and G on pages 37-42 of this report.

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

- Unemployment rates are not available for the City, however unemployment for Essex County where the City is located averaged 5.0 – 5.9% during 2002, which is consistent with the Commonwealth's rate of 5.2% and the National average rate of 5.8%.
- The occupancy rate of the government's central business district has remained at 65 – 70 percent for the past three years.
- Inflationary trends in the region are consistent with national indices.

All of these factors were considered in preparing the City's budget for the 2003 fiscal year.

During the current fiscal year, unreserved fund balance in the general fund decreased to \$4.6 million. The City has appropriated \$0.7 million of this amount for spending in the 2003 fiscal year budget. Additionally, the City will use \$0.7 million from recreation revolving funds and \$1.4 million from water and sewer enterprise to cover indirect costs. The City also has the ability to levy additional taxes without the need for an override or exemption, due to nearly \$0.8 million in excess levy capacity. As a result, the City's budget was in balance for the fiscal year 2003. Accordingly, the Commonwealth certified the tax-rate for 2003 in December 2002.

Water and Sewer rates were increased for fiscal 2003 to more adequately accommodate the costs and capital maintenance of this activity.

In the City's General Operating fund, property taxes represent 57% of the annual operating budget and local-aid from the Commonwealth represents 28% of the budget. Subsequent to the balance sheet date, the Commonwealth announced that it is expected to experience a double-digit deficit for fiscal year 2003 and it anticipates being about \$3 billion short on its fiscal 2004 budget. This has occurred due to a loss of significant income tax and sales tax revenue as a consequence to the deterioration in the overall health of the region's economy in recent years. As part of the Governor's stopgap measure to cover this deficit, significant cuts have been made in local-aid to Cities and Towns. It is anticipated that the City's local-aid for 2003 will be cut by 2.5% (approximately \$0.8 million) and local-aid for 2004 by 15 to 20% (approximately \$3 to \$4 million). There are no assurances that the amount of cuts won't ultimately be greater than these estimated balances as the Commonwealth strives to balance its own budget. The City will prepare its 2004 budget based on these assumptions. The City is presently reviewing all its options to mitigate the impact of the lost local-aid and these plans could include layoffs, reduction in services, increase in user charges and property taxes, appropriation from reserves or some combination of all of these. This is an ongoing process, as avoiding further major fiscal crisis and enduring this period of uncertainty is the City's most pressing imminent priority.

### **Requests for Information**

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Office of the Finance Director, 93 Washington Street Salem, Massachusetts, 01970.

## CITY OF SALEM, MASSACHUSETTS

## STATEMENT OF NET ASSETS

JUNE 30, 2002

	Governmental Activities	Business-Type Activities	Total
<b>ASSETS</b>			
<b>CURRENT:</b>			
Cash and cash equivalents	\$ 19,593,190	\$ 2,156,785	\$ 21,749,975
Investments	7,536,944		7,536,944
Receivables, net of allowance for uncollectibles:			
Real estate and personal property taxes	928,723		928,723
Tax liens	796,288		796,288
Motor vehicle excise	703,328		703,328
User fees		1,299,454	1,299,454
Departmental and other	172,403		172,403
Intergovernmental	5,602,098		5,602,098
Current portion of loans			
<b>Total Current Assets</b>	<b>35,332,974</b>	<b>3,456,239</b>	<b>38,789,213</b>
<b>NONCURRENT:</b>			
Restricted:			
Cash	1,757,071		1,757,071
Investments	3,000,724		3,000,724
Investment in joint venture		2,397,068	2,397,068
Receivables, net of allowance for uncollectibles:			
Intergovernmental	44,862,151		44,862,151
Long term portion of loans	1,187,885		1,187,885
Capital assets, net of accumulated depreciation	67,493,014	5,932,331	73,425,345
<b>TOTAL ASSETS</b>	<b>153,633,819</b>	<b>11,785,638</b>	<b>165,419,457</b>
<b>LIABILITIES</b>			
<b>CURRENT:</b>			
Warrants and accounts payable	6,287,993	241,237	6,529,230
Accrued expense	891,699		891,699
Interest expense	523,959		523,959
Retainage	312,535		312,535
Deposits	391,198	5,469	396,667
Tax refunds payable	27,723		27,723
Bond anticipation notes payable	14,500,000		14,500,000
Compensated absences	384,545		384,545
Risk financing	47,085		47,085
Current portion of debt	3,586,559	135,000	3,721,559
<b>Total Current Liabilities</b>	<b>26,953,296</b>	<b>381,706</b>	<b>27,335,002</b>
<b>NONCURRENT:</b>			
Bond and note indebtedness	56,771,000	515,000	57,286,000
Compensated absences	3,460,905		3,460,905
Risk financing	423,764		423,764
Capital leases	397,427		397,427
<b>TOTAL LIABILITIES</b>	<b>88,006,392</b>	<b>896,706</b>	<b>88,903,098</b>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	55,158,773	5,282,331	60,441,104
Restricted for			
Capital projects	(5,563,082)		(5,563,082)
Perpetual funds			
Expendable	3,137,654		3,137,654
Nonexpendable	1,430,279		1,430,279
Loans	1,187,884		1,187,884
Other purposes		2,397,068	2,397,068
Unrestricted	10,275,919	3,209,533	13,485,452
<b>NET ASSETS</b>	<b>\$ 65,627,427</b>	<b>\$ 10,888,932</b>	<b>\$ 76,516,359</b>

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

CITY OF SALEM, MASSACHUSETTS

STATEMENT OF ACTIVITIES  
FISCAL YEAR ENDED JUNE 30, 2002

FUNCTIONS/PROGRAMS	Expenses	Indirect Expenses Allocation	Program Revenues			Net (Expenses) Revenues and Changes in Net Assets		
			Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
<b>Governmental Activities:</b>								
General government	\$ 4,847,576		\$ 429,591	\$ 2,500	\$ 75,000	\$ (4,340,485)		\$ (4,340,485)
Public safety	13,493,638		1,323,642	775,536		(13,394,460)		(13,394,460)
Education	48,559,747		1,216,334	39,934,078		(7,409,335)		(7,409,335)
Public works	4,430,303		364,132	119,996	611,833	(3,334,342)		(3,334,342)
Health and human services	1,067,989		136,905	3,798,675		2,867,591		2,867,591
Culture and recreation	2,709,844		327,426	143,736	170,724	(2,067,958)		(2,067,958)
Pension benefits	8,505,513			4,301,287		(4,204,226)		(4,204,226)
Fringe benefits	9,955,313			2,327,719		(7,627,594)		(7,627,594)
State and County charges	3,770,566					(3,770,566)		(3,770,566)
Debt service	3,046,692		231,169	3,676,179		629,487		629,487
Community development	5,856,034			2,247,619		(3,377,246)		(3,377,246)
<b>Total Governmental Activities</b>	<b>108,243,215</b>	<b>\$ -</b>	<b>4,029,199</b>	<b>57,327,325</b>	<b>857,557</b>	<b>(46,029,134)</b>	<b>\$ -</b>	<b>(46,029,134)</b>
<b>Business-Type Activities:</b>								
Water and sewer services	10,967,114		9,794,892				(1,172,222)	(1,172,222)
Golf course	387,935		615,878				227,943	227,943
Parking	719,042		1,270,928				551,886	551,886
<b>Total Primary Government</b>	<b>\$ 120,317,306</b>		<b>\$ 15,710,897</b>	<b>\$ 57,327,325</b>	<b>\$ 857,557</b>	<b>(46,029,134)</b>	<b>(392,393)</b>	<b>(46,421,327)</b>
<b>General Revenues:</b>								
Real and personal property taxes						49,486,747		49,486,747
Motor vehicle and other excise						3,626,065		3,626,065
Penalties and interest on taxes						330,035		330,035
Intergovernmental						3,931,117		3,931,117
Investment income						125,481		125,481
Other						504,968		504,968
Transfers (net)						2,274,567	(2,274,567)	-
<b>Total general revenues and transfers</b>						<b>60,278,980</b>	<b>(2,274,567)</b>	<b>58,004,413</b>
<b>Change in Net Assets</b>						<b>14,249,846</b>	<b>(2,666,960)</b>	<b>11,582,886</b>
<b>Net Assets:</b>								
Beginning of year						51,377,581	13,555,892	64,933,473
End of year						<b>\$ 65,627,427</b>	<b>\$ 10,888,932</b>	<b>\$ 76,516,359</b>

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



## CITY OF SALEM, MASSACHUSETTS

## GOVERNMENTAL FUNDS

## BALANCE SHEET

JUNE 30, 2002

	General	Stabilization	Nonmajor Governmental Funds	Total Governmental Funds
<b>ASSETS</b>				
Cash and short-term investments	\$ 9,132,306	\$ 2,248,337	\$ 8,212,547	\$ 19,593,190
Investments			7,536,944	7,536,944
Receivables, net of allowance for uncollectibles				
Real estate and personal property taxes	928,723		1,187,885	2,116,608
Other	1,505,169		166,850	1,672,019
Due from other government	28,887,290		2,545,559	31,432,849
Cash - restricted			1,757,071	1,757,071
Investments - restricted			3,000,724	3,000,724
<b>Total Assets</b>	<b>\$ 40,453,488</b>	<b>\$ 2,248,337</b>	<b>\$ 24,407,580</b>	<b>\$ 67,109,405</b>
<b>LIABILITIES AND FUND BALANCES</b>				
<b>LIABILITIES:</b>				
Warrants and accounts payable	\$ 2,927,170		\$ 3,360,822	\$ 6,287,992
Accrued expenses	523,959			523,959
Retainage payable			312,535	312,535
Other liabilities	391,198			391,198
Tax refunds payable	27,723			27,723
Deferred revenues	30,507,978		1,187,885	31,695,863
Bond anticipation notes payable			35,646,000	35,646,000
<b>Total Liabilities</b>	<b>34,378,028</b>		<b>40,507,242</b>	<b>74,885,270</b>
<b>FUND BALANCES:</b>				
Reserved for:				
Encumbrances	1,442,182			1,442,182
Stabilization		\$ 2,248,337		2,248,337
Unreserved:				
Undesignated, reported in:				
General fund	4,633,278			4,633,278
Special revenue funds			6,041,486	6,041,486
Capital projects funds			(26,709,082)	(26,709,082)
Permanent funds			4,567,934	4,567,934
<b>Total Fund Balances</b>	<b>6,075,460</b>	<b>2,248,337</b>	<b>(16,099,662)</b>	<b>(7,775,865)</b>
<b>Total Liabilities and Fund Balances</b>	<b>\$ 40,453,488</b>	<b>\$ 2,248,337</b>	<b>\$ 24,407,580</b>	<b>\$ 67,109,405</b>

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

## CITY OF SALEM, MASSACHUSETTS

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

JUNE 30, 2002

	General	Stabilization	Nonmajor Governmental Funds	Total Governmental Funds
<b>REVENUES</b>				
Real estate and personal property taxes, net	\$ 50,152,793			\$ 50,152,793
Intergovernmental	29,966,021		\$ 14,285,129	44,251,150
Motor vehicle and other excises	3,156,366			3,156,366
Departmental and other revenue	1,635,992		2,090,831	3,726,823
License and permits	414,908			414,908
Penalties and interest on taxes	330,035			330,035
Fines and forfeitures	753,821			753,821
Investment income	630,270	\$ 34,523	(537,331)	127,462
Contributions and donations			2,675,111	2,675,111
Miscellaneous	221,865			221,865
Total Revenues	87,262,071	34,523	18,513,740	105,810,334
<b>OTHER FINANCING SOURCES</b>				
Transfers in	2,675,125	500,000	5,869,878	9,045,003
Total Other Financing Sources	2,675,125	500,000	5,869,878	9,045,003
Total Revenues and Other Financing Sources	89,937,196	534,523	24,383,618	114,855,337
<b>EXPENDITURES</b>				
General government	4,141,832		724,399	4,866,231
Public safety	14,765,329		973,469	15,738,798
Education	38,795,102		17,511,207	56,306,309
Public works	4,522,789		129,956	4,652,745
Health and human services	960,817			960,817
Culture and recreation	2,406,424		322,046	2,728,470
Fringe Benefits	1,470,572		8,382,901	9,853,473
State and county tax assessments	3,770,566			3,770,566
Community development			5,856,034	5,856,034
Pensions	8,505,513			8,505,513
Debt service	5,631,786		85,000	5,716,786
Total Expenditures	84,970,730	-	33,985,012	118,955,742
<b>OTHER FINANCING USES</b>				
Transfers out	6,225,225		545,211	6,770,436
Total Expenditures and Other Financing Uses	91,195,955	-	34,530,223	125,726,178
<b>EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES</b>				
	(1,258,759)	534,523	(10,146,605)	(10,870,841)
FUND BALANCES, JULY 1, 2001	7,334,219	1,713,814	(5,953,057)	3,094,976
FUND BALANCES, JUNE 30, 2002	\$ 6,075,460	\$ 2,248,337	\$ (16,099,662)	\$ (7,775,865)

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

CITY OF SALEM, MASSACHUSETTS

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

JUNE 30, 2002

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Total Governmental Fund Balances	\$ (7,775,865)
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	67,493,014
Other long-term assets are not available to pay for current-period expenditures and are therefore deferred on funds.	31,695,863
Short-term obligations that are refinanced subsequent to the balance sheet date are to be classified as long-term liabilities. The net impact on Bond anticipation notes payable, long-term obligations, and the receivable due from intergovernmental due to different accounting treatment.	19,031,400
In the statement of activities, interest is accrued on outstanding long-term debt, whereas in governmental funds interest is not reported until due.	(891,699)
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the government funds:	
Bonds and notes payable	(38,505,000)
Capital leases	(1,103,987)
Compensated absences	(3,845,450)
Risk financing activities	<u>(470,849)</u>
Net Assets of Governmental Activities	<u>\$ 65,627,427</u>

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

CITY OF SALEM, MASSACHUSETTS

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

JUNE 30, 2002

Net Change in Fund Balances - Total Governmental Fund Balances \$ (10,870,841)

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 outlays amounted to \$9,673,645 and depreciation expense totaled \$2,344,501. The net amount is reflected here as a reconciling item. 7,329,144

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the financial resources of governmental funds. Neither has any effect on net assets. Also governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. Debt repayments were \$2,690,000 and proceeds were \$0. The net amount is reflected here as a reconciling item. 2,690,000

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 differ between the two statements. The amount presented represents the difference in deferred revenue. (4,623,240)

Revenues in the Statement of activities that relate to the conversion of short-term debt to long-term liabilities and the resultant receivable from the Commonwealth of Massachusetts due to the School Business Assistance Program are not reflected in the Statement of Revenues, Expenditures and Changes in Fund Balances. 19,031,400

In the statement of activities, interest is accrued on outstanding long-term debt, whereas in governmental funds interest is not reported until due. This represents the difference between the accruals between this year and the prior year. (19,906)

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:

Capital leases	815,129
Compensated absences	-
Risk financing	(101,840)

Change in Net Assets of Governmental Activities \$ 14,249,846

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

## CITY OF SALEM, MASSACHUSETTS

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE**  
**BUDGET AND ACTUAL - GENERAL FUND**  
**YEAR ENDED JUNE 30, 2002**

	Budgeted Amounts		Actual	Variance
	Original	Final	Budgetary	Favorable
	Budget	Budget	Amounts	(Unfavorable)
<b>REVENUES</b>				
Real estate and personal property taxes, net	\$ 50,054,415	\$ 50,054,415	\$ 50,152,793	\$ 98,378
Intergovernmental	25,845,371	25,845,371	25,690,352	(155,019)
Motor vehicle and other excises	3,215,825	3,215,825	3,156,366	(59,459)
Departmental and other revenue	1,397,312	1,397,312	1,635,992	238,680
License and permits	420,293	420,293	414,908	(5,385)
Penalties and interest on taxes	418,816	418,816	330,035	(88,781)
Fines and forfeitures	712,592	712,592	753,821	41,229
Investment income	950,000	950,000	630,270	(319,730)
Miscellaneous	108,123	108,123	221,865	113,742
Total Revenues	83,122,747	83,122,747	82,986,402	(136,345)
<b>EXPENDITURES</b>				
General government	4,042,832	4,418,269	4,141,832	276,437
Public safety	14,378,856	15,047,764	14,765,329	282,435
Education	39,629,142	39,892,217	38,795,102	1,097,115
Public works	5,309,296	5,309,296	4,522,789	786,507
Health and human services	866,418	998,500	960,817	37,683
Culture and recreation	2,753,783	2,876,925	2,406,424	470,501
Fringe Benefits	1,547,940	1,547,940	1,470,572	77,368
State and county tax assessments	3,861,477	3,861,477	3,770,566	90,911
Pensions	4,243,230	4,243,230	4,229,844	13,386
Debt service	5,869,963	5,869,963	5,631,786	238,177
Total Expenditures	82,502,937	84,065,581	80,695,061	3,370,520
<b>OTHER FINANCING SOURCES (USES)</b>				
Transfers in	2,675,125	2,675,125	2,675,125	-
Transfers out	(6,225,225)	(6,225,225)	(6,225,225)	-
Total Other Financing Sources (Uses)	(3,550,100)	(3,550,100)	(3,550,100)	-
<b>EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES/USE OF PRIOR YEAR BUDGETARY FUND BALANCE</b>				
	(2,930,290)	(4,492,934)	(1,258,759)	3,234,175
BUDGETARY FUND BALANCES, JULY 1, 2001	6,141,964	6,141,964	6,141,964	-
BUDGETARY FUND BALANCES, JUNE 30, 2002	<u>\$ 3,211,674</u>	<u>\$ 1,649,030</u>	<u>\$ 4,883,205</u>	<u>\$ 3,234,175</u>

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

## CITY OF SALEM, MASSACHUSETTS

**PROPRIETARY FUNDS**  
**STATEMENT OF NET ASSETS**  
**JUNE 30, 2002**

	Business-type Activities - Enterprise Funds			
	Water and Sewer	Golf Course	Parking Activities	Totals
<b>ASSETS</b>				
<b>CURRENT:</b>				
Cash and cash equivalents	\$ 1,859,597	\$ 297,188		\$ 2,156,785
User fees, net of allowance for uncollectibles	1,299,454			1,299,454
<b>Total Current Assets</b>	<b>3,159,051</b>	<b>297,188</b>	<b>\$ -</b>	<b>3,456,239</b>
<b>NONCURRENT:</b>				
Capital assets, net of accumulated depreciation	222,845	621,353	5,088,133	5,932,331
Investment in joint venture	2,397,068			2,397,068
<b>TOTAL ASSETS</b>	<b>5,778,964</b>	<b>918,541</b>	<b>5,088,133</b>	<b>11,785,638</b>
<b>LIABILITIES</b>				
<b>CURRENT:</b>				
Warrants and accounts payable	241,237			241,237
Deposits	5,469			5,469
Current portion of debt	105,000	30,000		135,000
<b>Total Current Liabilities</b>	<b>351,706</b>	<b>30,000</b>	<b>-</b>	<b>381,706</b>
<b>NONCURRENT:</b>				
Long term portion of debt	105,000	410,000		515,000
<b>TOTAL LIABILITIES</b>	<b>456,706</b>	<b>440,000</b>	<b>-</b>	<b>896,706</b>
<b>NET ASSETS</b>				
Invested in capital assets, net of related debt	12,845	181,353	5,088,133	5,282,331
Investment in joint venture	2,397,068			2,397,068
Unrestricted	2,912,345	297,188		3,209,533
<b>NET ASSETS</b>	<b>\$ 5,322,258</b>	<b>\$ 478,541</b>	<b>\$ 5,088,133</b>	<b>\$ 10,888,932</b>

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

## CITY OF SALEM, MASSACHUSETTS

**PROPRIETARY FUNDS**  
**STATEMENT OF REVENUES, EXPENSES,**  
**AND CHANGES IN FUND NET ASSETS**  
**YEAR ENDED JUNE 30, 2002**

	Business-type Activities - Enterprise Funds			
	Water and Sewer	Golf Course	Parking Activities	Totals
<b>OPERATING REVENUES</b>				
Charges for services	\$ 9,794,892	\$ 615,878	\$ 1,270,928	\$ 11,681,698
Total Operating Revenues	9,794,892	615,878	1,270,928	11,681,698
<b>OPERATING EXPENSES</b>				
Operation costs	10,659,167	337,085	528,549	11,524,801
Depreciation	2,999	28,112	190,493	221,604
Net activity of joint venture	291,298			291,298
Total Operating Expenses	10,953,464	365,197	719,042	12,037,703
<b>OPERATING INCOME</b>	(1,158,572)	250,681	551,886	(356,005)
<b>NONOPERATING REVENUES (EXPENSES):</b>				
Interest expense	(13,650)	(22,738)		(36,388)
Transfers out	(1,367,011)	(165,177)	(742,379)	(2,274,567)
Total Nonoperating Revenues (Expenses), net	(1,380,661)	(187,915)	(742,379)	(2,310,955)
<b>CHANGE IN NET ASSETS</b>	(2,539,233)	62,766	(190,493)	(2,666,960)
<b>NET ASSETS AT BEGINNING OF YEAR</b>	7,861,491	415,775	5,278,626	13,555,892
<b>NET ASSETS AT END OF YEAR</b>	<u>\$ 5,322,258</u>	<u>\$ 478,541</u>	<u>\$ 5,088,133</u>	<u>\$ 10,888,932</u>

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

## CITY OF SALEM, MASSACHUSETTS

**PROPRIETARY FUNDS  
STATEMENT OF CASH FLOWS -  
YEAR ENDED JUNE 30, 2002**

	Business-type Activities - Enterprise Funds			
	Water and Sewer	Golf Course	Parking Activities	Totals
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>				
Receipts from users	\$ 10,301,350	\$ 615,878	\$ 1,270,928	\$ 12,188,156
Payments to vendors	(9,867,731)	(123,327)	(142,597)	(10,133,655)
Payments to employees	(673,764)	(213,758)	(385,952)	(1,273,474)
<b>Net Cash Provided by (Used for) Operating Activities</b>	<b>(240,145)</b>	<b>278,793</b>	<b>742,379</b>	<b>781,027</b>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>				
Transfers out	(1,367,011)	(165,177)	(742,379)	(2,274,567)
<b>Net Cash Used for Noncapital Related Financing Activities</b>	<b>(1,367,011)</b>	<b>(165,177)</b>	<b>(742,379)</b>	<b>(2,274,567)</b>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>				
Proceeds from the issuance of bonds and notes				-
Acquisition and construction of capital assets				-
Principal payments on bonds and notes	(170,000)	(30,000)		(200,000)
Interest expense	(13,650)	(22,738)		(36,388)
<b>Net Cash Used for Capital and Related Financing Activities</b>	<b>(183,650)</b>	<b>(52,738)</b>	<b>-</b>	<b>(236,388)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>				
Investment income		-	-	-
<b>Net Cash Provided by Investing Activities</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>NET CHANGE IN CASH AND EQUIVALENTS</b>	<b>(1,790,806)</b>	<b>60,878</b>	<b>-</b>	<b>(1,729,928)</b>
<b>CASH AND EQUIVALENTS:</b>				
July 1, 2001	3,650,403	236,310	-	3,886,713
June 30, 2002	<u>\$ 1,859,597</u>	<u>\$ 297,188</u>	<u>\$ -</u>	<u>\$ 2,156,785</u>
	3,650,403	236,310	0	
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES:</b>				
Operating income (loss)	\$ (1,158,572)	\$ 250,681	\$ 551,886	\$ (356,005)
Depreciation	2,999	28,112	190,493	221,604
Changes in assets and liabilities:				
Receivables (net)	506,458			506,458
Joint venture	291,298			291,298
Accounts payable	117,672			117,672
<b>Net Cash Provided From Operating Activities</b>	<b>\$ (240,145)</b>	<b>\$ 278,793</b>	<b>\$ 742,379</b>	<b>\$ 781,027</b>
<b>NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES:</b>				
Borrowing under capital leases	-	-	-	-
Contributions of capital assets from General Fund	-	-	-	-
Purchase of equipment on account	-	-	-	-
Increase in fair value of investments	-	-	-	-
Capital asset trade-ins	-	-	-	-

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



## CITY OF SALEM, MASSACHUSETTS

**FIDUCIARY FUNDS**  
**STATEMENT OF FIDUCIARY NET ASSETS**  
**JUNE 30, 2002**

	Pension Trust Fund (As of December 31, 2001)	Private Purpose Trust Funds
<b>ASSETS</b>		
<b>CURRENT:</b>		
Cash and Cash Equivalents	\$ 3,710,962	\$ 73,637
Investments (at fair value):		
Fixed income securities	24,876,789	
Equity securities	17,019,958	
Pooled Funds:		
Domestic Equity	7,561,075	
International Equity	5,435,934	
Real Estate	4,575,398	
Venture Capital	6,802,863	
Mutual funds		1,148,535
Total Investments	66,272,017	1,148,535
Receivables:		
Dividends and interest	393,624	
Employer contributions	75,353	
Member deductions	19,238	
Commonwealth of Massachusetts	518,930	
Total Receivables	1,007,145	-
<b>Total Assets</b>	<b>70,990,124</b>	<b>1,222,172</b>
<b>LIABILITIES</b>		
<b>CURRENT:</b>		
Accounts payable and accrued expenses	109,252	
Due to other government	20,503	
<b>Total Liabilities</b>	<b>129,755</b>	<b>-</b>
<b>NET ASSETS</b>		
Held in trust for pension benefits and other purposes	70,860,369	1,222,172
<b>Net Assets</b>	<b>\$ 70,860,369</b>	<b>\$ 1,222,172</b>

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

**CITY OF SALEM, MASSACHUSETTS**

**FIDUCIARY FUNDS  
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS  
YEAR ENDED JUNE 30, 2002**

	Pension Trust Fund (As of December 31, 2001)	Private Purpose Trust Funds
<b>ADDITIONS:</b>		
Contributions:		
Employer	\$ 4,756,276	
Employee	2,450,653	
From Commonwealth of Massachusetts	641,672	
Transfers from other systems	100,612	
Reimbursements from other systems	87,902	
From federal grant	9,337	
Donations		\$ 3,867
Investment Income	3,099,945	
Net gain (loss) on investments (including realized and unrealized gains and losses)	(4,630,505)	(125,273)
<b>Total Additions</b>	<b>6,515,892</b>	<b>(121,406)</b>
<b>EXPENDITURES:</b>		
Benefit payments to retirees and surviving spouses	8,147,918	
Refunds:		
Members	235,433	
Option B	21,428	
Reimbursements to other systems	170,445	
Transfers to other systems	262,463	
Payroll expenses of the System	143,076	
Other administrative expenses	482,774	
Scholarships and assistance		65,439
<b>Total Deductions</b>	<b>9,463,537</b>	<b>65,439</b>
<b>CHANGE IN NET ASSETS</b>	<b>(2,947,645)</b>	<b>(186,845)</b>
<b>NET ASSETS AT BEGINNING OF YEAR</b>	<b>73,808,014</b>	<b>1,409,017</b>
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 70,860,369</b>	<b>\$ 1,222,172</b>

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

## CITY OF SALEM, MASSACHUSETTS

### NOTES TO BASIC FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2002

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#### I. Summary of Significant Accounting Policies

The basic financial statements of the City, have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to state and local governments. GAAP is prescribed by the Governmental Accounting Standards Board (GASB), which is the primary standard-setting body for state and local government entities. In June 1999 the GASB issued Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – For State and Local Governments. Statement No. 34 makes the most significant changes in governmental financial reporting in over twenty years. The requirements of Statement No. 34 are not mandatory for the City until the fiscal year ended June 30, 2003 however the City has made the decision to early implement the Statement’s requirements effective June 30, 2002. The following is a summary of the more significant policies and practices used by the City:

- A. **Reporting Entity** - The City of Salem is located in Essex County, sixteen miles northeast of Boston. Salem was incorporated as a town in 1630 and established as a city in 1836. An elected Mayor who serves a four-year term and an eleven-member City Council who are elected biennially govern the City. The City provides governmental services for the territory within its boundaries, including police and fire protection, disposal of garbage and rubbish, public education in grades K-12, water and sewer services, street maintenance, parks and recreational facilities. Water and sewer services, funded almost entirely with user charges are provided via connections to the Salem and Beverly Water Supply Board (the Supply Board) and the South Essex Sewerage District (the District).
- B. **Individual Component Unit Disclosures** - The following component unit is, while a separate entity, in substance part of the governmental operations of the City due to the significance of its operations and financial relationship with the City. Data is blended with City data as the primary government.

South Essex Sewerage District – The District is a joint venture servicing Salem, Peabody, Beverly, Danvers and Marblehead, established for the operation of a septic disposal facility. Each member community is responsible for their proportionate share of the operational costs of the District, which are paid in the form of assessments. At June 20, 2002, the City has an equity unreserved and undesignated in the operations of the District of \$2,397,068. This activity is reflected in the City’s Business-Type activities.

- C. **Government-Wide and Fund Financial Statements** – The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its component units. 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 legal *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 are 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 or 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*. Separate financial statements are provided for Governmental Funds, proprietary funds, and fiduciary funds, even though the latter are excluded from government-wide financial statements. Major individual Governmental Funds are reported as separate columns in the fund financial statements.

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

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**I. Summary of Significant Accounting Policies (continued)**

- D. Measurement Focus, Basis of Accounting, and Financial Statement Presentation** – The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are proprietary funds 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. 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 revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However expenditures related to debt service, compensated absences, claims and judgments, and risk financing, are recorded only when payment is due. Property taxes, licenses, and interest associated with the current fiscal period are all considered being susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

The government reports the following major Governmental Funds:

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.

Stabilization Fund – is used to account for certain unencumbered accumulated financial resources that are subject to appropriation as directed by the City's Legislative branch. These funds are typically used for nonrecurring expenditures, usually capital in nature or unexpected items that may arise during the year.

The government reports the following major proprietary funds:

Enterprise Fund – uses the "economic resources" measurement focus to account for the following specific operations in a manner similar to private business enterprises:

Water and Sewer – accounts for user charges collected to finance costs associated with maintaining the related infrastructure within the City boundaries, and fund the assessments charged by the Salem and Beverly Water Board and South Essex Sewerage District for maintaining the facilities by which the water and sewage is processed.

Golf Course – accounts for the operations of the City's 9-hole golf course facility, which is maintained through the collection of user fees. Certain receipts are utilized to supplement the Parks and Recreation appropriation in the General Fund.

Parking Activities – accounts for the activities associated with maintaining the City's parking garages, lots, and metered spaces through the collection of parking fees.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

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**I. Summary of Significant Accounting Policies (continued)**

**D. Measurement Focus, Basis of Accounting, and Financial Statement Presentation (continued)**

Additionally, the government reports the following fund types:

*Private-Purpose Trust Fund* – is used to account for resources legally held in trust for use in funding scholarships and energy support for qualified citizens. There is a requirement that a portion of these resources be preserved as capital.

*Pension Trust Fund* – substantially all employees of the City, except teachers and certain administrative personnel employed by the School Department participate in the Salem Contributory Retirement System (the Retirement System). The Retirement System functions for the benefit of these employees.

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 to the extent that those standards do not conflict with or contradict guidance of the GASB. Governments also have the *option* of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to the same limitation. The City has elected not to follow private-sector guidance. As a general rule the *effect* of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments in lieu of taxes and other charges between the City's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned. Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise general revenues include all taxes. Proprietary funds distinguish *operating* revenues and expenses from *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 funds are charges to customers for sales and services. Operating expenses for the enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues not meeting this definition are reported as non-operating revenues and expenses. When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources, as they are needed.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

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I. Summary of Significant Accounting Policies (continued)

E. Assets, Liabilities, and Net Assets or Equity

Deposits and Investments – The City's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

State statutes authorize the City to invest in obligations of the United States Treasury, commercial paper, corporate bonds, repurchase agreements and the State Treasurer's Investment Pool. Investments for the City, the Retirement System, and its component units are reported at fair value. The State Treasurer's Investment Pool operates in accordance with state laws and regulations. The reported value of the pool is the same as the fair value of the pool shares.

Interfund Balances – Activity between funds that are representative of lending arrangements outstanding at the end of the fiscal year are referred to as either *due to/from other funds* or *advances to/from other funds*. All other outstanding balances between funds are reported as due to/from other funds.

Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as *internal balances*.

Receivables – All property tax and trade receivables are shown net of an allowance for doubtful collections comprised of those outstanding amounts greater than five years old. Real estate and personal property taxes are assessed on January 1 every year. Bills are sent quarterly and are due on July 1, October 1, January 1, and April 1, or thirty days subsequent to the mailing date. Interest accrues on delinquent taxes to the rate of 14% per annum. The City is allowed to take delinquent tax accounts into tax title fourteen days subsequent to the mailing of demand of delinquent taxes.

Mortgage receivables are principally comprised of funds advanced to developers under various Urban Development Action Grants (UDAG) and Residential Rehabilitation agreements. The City loans funds to owners of commercial and residential properties for the purpose of rehabilitating these properties. The City receives these funds from the U.S. Department of Housing and Urban Development (HUD) under Community Development Block Grant (CDBG) programs for the City, and from loan repayments. These loans are repaid to the City under various terms and conditions stipulated by each mortgage agreement. The collected proceeds of these loans may be used for any eligible activity relevant to the community development program.

Inventories and Prepaid Items – Inventories, which are not material to the basic financial statements, are considered to be expenditures at the time of purchase.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Restricted Assets – Certain cash and investment balances are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by the provisions of certain trust documents.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

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I. Summary of Significant Accounting Policies (continued)

E. Assets, Liabilities, and Net Assets or Equity (continued)

Capital Assets – Capital assets, which include property, plant, and equipment are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two 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 City has elected not to capitalize infrastructure assets until required in 2006.

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. The total interest expense incurred by the City during the current fiscal year was \$2,504,944. None of this was considered construction period interest.

Property, plant and equipment of the primary government as well as the component units is depreciated using the straight line method over the following estimated useful lives:

Structures and improvements	40 years
Equipment, furniture, fixtures and vehicles	5 years

Compensated Absences – It is the City's policy to permit employees to accumulate earned but unused vacation and sickpay benefits. Amounts related to these benefits are 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.

Long-term Obligations – In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs are deferred and amortized over the life of the bonds. Bond anticipation notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, Governmental Fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on a debt issuance are reported as other financing sources while discounts as other financing uses. Issuance costs are exclusively reported as debt service expenditures regardless of whether they are withheld from the actual proceeds.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

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**I. Summary of Significant Accounting Policies (continued)**

**E. Assets, Liabilities, and Net Assets or Equity (continued)**

Deferred Mortgage Revenue – Deferred mortgage revenue of the City is recorded when loans collateralized by real estate are originated. Such amounts are reclassified to revenue upon repayment.

Risk Financing – The City does not insure for workers' compensation, health, or unemployment benefits. The City does insure for casualty, theft, or other losses. Uninsured losses are recorded as expenditures when incurred. Amounts determined to be incurred but not reported are reflected as liabilities of the Government-Wide Statement of Net Assets.

Encumbrances – Encumbrance accounting, under which purchase orders, contracts and other commitments for expenditure of funds are recorded in order to reserve that portion of the applicable appropriation, is employed as a significant aspect of budgetary control in the Governmental Fund types. Encumbrances outstanding at year-end are reported as reservations of fund balances, since they do not constitute expenditures or liabilities.

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.

**II. Stewardship, Compliance and Accountability**

- A. Budgetary Information** – An annual budget is legally adopted for the General Fund and the Enterprise Fund. Financial orders are initiated by department heads, recommended by the Mayor and approved by the City Council at the City's annual meeting in June. Expenditures may legally exceed appropriations at the department level. Department heads may transfer, without City Council approval, appropriation balances from one expenditure account to another within their department or budget. The City Council and the department head however must approve any transfer of unencumbered appropriation balances between departments or agencies. At the close of each fiscal year, unencumbered appropriation balances lapse or reverts to unreserved fund balance. The City made several supplemental budgetary appropriations throughout the year approximating \$2.5 million. The majority of these were to supplement the City's individual appropriations.
- B. Excess of Expenditures Over Appropriations** – During the fiscal year ended, expenditures exceeded appropriations for certain State and County assessments. The over-expenditure was funded on the 2003 tax recapitulation sheet.
- C. Deficit Fund Equity** – The City incurred legal deficits in its Capital Projects Fund in the amount of \$26,709,082 that will be raised through future bond issuance.



**CITY OF SALEM, MASSACHUSETTS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002**

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**III. Detailed Notes to All Funds**

- A. Deposits and Investments** – Cash and equivalents include cash on hand and certificates of deposit with maturities of three months or less.

The City maintains a separate cash accounts for all funds, except the Pension Trust Fund. In addition, certificates of deposit and investments are held separately by the Permanent Funds. The deposits and investments of the Pension Trust Fund are held separately from those of other funds and are covered by federal depository insurance and government securities.

At year-end, the carrying amount of the City's deposits was \$13,568,466 and the bank balance was \$11,587,177. Of the City's bank balance, \$300,000 was covered by federal depository insurance; \$5,372,949 by depositors insurance fund; and the remaining \$5,914,228 was collateralized.

At December 31, 2001, the carrying amount of deposits for the Pension Trust Fund was \$50,779 and the bank balance was \$250,000. Of the bank balance, \$100,000 was covered by federal depository insurance and the remaining \$150,000 by depositors insurance fund.

Statutes require the Treasurer to invest City funds in bonds or notes which are legal investments for savings banks, including U.S. obligations, certificates of deposit, money market accounts, bank deposits, repurchase agreements and the State Treasurer's investment pool. In addition, the statutes impose various limitations on the amount and length of investments and deposits. Repurchase agreements cannot be for a period of over ninety days, and the underlying security must be an U.S. obligation. During the fiscal year, the City did not enter into any repurchase agreements. The Retirement System has received a waiver from the Commonwealth of Massachusetts relative to these statutes.

The fair value of bonds and government obligations were determined, based on quoted market prices. The fair values of stocks were determined by closing prices for those securities traded on national stock exchanges and at the average of bid-and-asked quotations for these securities traded in the over-the-counter market.

From time to time, the Pension Trust Fund may invest in derivative products, mainly currency hedges, to minimize currency risk on international investments. Professional money managers whose investment performance is subject to periodic review manage these investments. The City believes its exposure to derivatives to be insignificant.

In accordance with GAAP, investments as detailed in the following paragraphs are classified as to credit risk by the three categories described below:

- Category 1: Insured or registered, or securities held by the City or its agent in the City's name.
- Category 2: Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the City's name.
- Category 3: Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the City's name.

## CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

## III. Detailed Notes to All Funds (continued)

## A. Deposits and Investments (continued)

	Category 1	Category 2	Category 3	Fair Value
<b>City at June 30, 2002:</b>				
U.S. Government obligations	\$ 7,536,944			\$ 7,536,944
Fixed income securities	1,743,511			1,743,511
Equity securities	2,196,015			2,196,015
	<u>11,476,470</u>			<u>11,476,470</u>
Investments not subject to categorization:				
State Treasurer's Investment Pool				2,277,828
Money Markets				6,712,558
Mutual Fund				209,733
Certificates of Deposit				<u>1,072,610</u>
Total City funds				<u>21,749,199</u>
<b>Pension Trust Fund at December 31, 2001:</b>				
U.S. Government obligations		6,569,731		6,569,731
Fixed income securities		18,307,058		18,307,058
Equity securities		17,019,958		17,019,958
		<u>41,896,747</u>		<u>41,896,747</u>
Investments not subject to categorization:				
Money Markets				3,660,183
Mutual funds				12,997,009
Real estate				4,575,398
Venture capital				<u>6,802,863</u>
Total Pension Trust Fund				<u>69,932,200</u>
Total				<u>\$ 91,681,399</u>
Following is a reconciliation of investments and cash and equivalents as summarized above to the balance as recorded in the combined balance sheet:				
		<u>Investments</u>	<u>Cash and Equivalents</u>	
As presented above		\$ 91,681,399	\$ 13,568,466	
Reclass: Short-term investments reported in the combined balance sheet as cash and short-term investments; As follows:				
Money Market investments		(10,372,741)	10,372,741	
Certificates of Deposit (Short-Term)		(1,072,610)	1,072,610	
State Treasurer's Investment Pool		<u>(2,277,828)</u>	<u>2,277,828</u>	
Totals		<u>\$ 77,958,220</u>	<u>\$ 27,291,645</u>	

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2002

III. Detailed Notes to All Funds (continued)

B. Receivables

*Presentation Breakdown* – Receivables as of year-end for the government's individual major, proprietary and fiduciary funds in the aggregate, including applicable allowances for uncollectible accounts, are as follows:

	General	Nonmajor	Water and Sewer	Retirement System	Total
Property taxes	\$ 1,055,367				\$ 1,055,367
Tax liens	796,288				796,288
Excise	799,235				799,235
User fees			\$ 1,299,454		1,299,454
Intergovernmental	28,887,290	\$ 2,545,559		\$ 518,930	31,951,779
Mortgages		1,762,568			1,762,568
Interest				393,624	393,624
Pension contributions				94,591	94,591
Other	5,554	166,850			172,404
Gross receivables	31,543,734	4,474,977	1,299,454	1,007,145	38,325,310
Allowance for Uncollectible accounts	( 222,552)	( 574,683)			( 797,235)
Net receivables	<u>\$ 31,321,182</u>	<u>\$ 3,900,294</u>	<u>\$ 1,299,454</u>	<u>\$ 1,007,145</u>	<u>\$ 37,528,075</u>

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. Governmental Funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, deferred revenue reported in Governmental Funds amounted to \$31,695,863. The City does not have any unearned revenue as of the end of the fiscal year.

*School Building Assistance Reimbursement* – As of June 30, 2002, the City expects to receive as the balance of grants from the Commonwealth of Massachusetts under Chapter 645 of the Acts of 1948, as amended, approximately \$40,291,853 applicable to approved school construction costs which includes both principal and interest. Such costs are reimbursed to the City in equal installments over the life (currently estimated at twenty years) of the related bond issues and are subject to appropriation only by the State Legislature. In the Governmental funds, the General Fund includes a receivable of \$28,285,359 under the caption Intergovernmental; this includes the reimbursable portion of the principal balance and the reimbursable portion of the accrued interest expense as of June 30, 2002. In the Statement of Net Assets, the Governmental Activities includes a receivable for \$44,862,151, which also includes \$19,031,400 that relates to temporary notes refinanced to bonds issued subsequent to year end that were included as long-term liabilities in the Statement of Net Assets.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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III. Detailed Notes to All Funds (continued)

B. Receivables (continued)

Mortgage Notes – The City has retained two banks to service various term loans executed 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 \$1,762,568 has been reflected as a receivable in the Nonmajor Governmental Funds. The interest on these loans varies between 0-8% and the loans mature on various dates through 2031.

C. Interfund Receivables, Payables and Transfers – Interfund transfers during the year were as follows:

	<u>Transfers In</u>	<u>Transfers Out</u>
General	\$ 2,675,125	\$ 6,225,225
Stabilization	500,000	
Nonmajor Governmental	5,869,878	545,211
Water & Sewer Business-Type		1,367,011
Golf Business-Type		165,177
Parking Business-Type		742,379
	<hr/>	<hr/>
Totals	<u>\$ 9,045,003</u>	<u>\$ 9,045,003</u>

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

III. Detailed Notes to All Funds (continued)

D. Capital Assets

Capital asset activity for the year ended June 30, 2002 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
<u>Governmental Activities:</u>				
Capital assets not being depreciated:				
Land	\$ 4,684,753			\$ 4,684,753
Construction in progress	1,894,449	4,068,810		5,963,259
Total capital assets not being depreciated	6,579,202	4,068,810	-	10,648,012
Capital assets being depreciated:				
Buildings and improvements	68,499,363	4,613,870		73,113,233
Improvements other than buildings	1,550,427	450,000		2,000,427
Machinery and equipment	2,811,957	185,384		2,997,341
Vehicles	5,687,616	355,581		6,043,197
Total capital assets being depreciated	78,549,363	5,604,835	-	84,154,198
Less accumulated depreciation for:				
Buildings and improvements	(18,835,210)		(1,685,444)	(20,520,654)
Improvements other than buildings	(863,770)		(64,952)	(928,722)
Machinery and equipment	(1,749,602)		(186,094)	(1,935,696)
Vehicles	(3,516,111)		(408,013)	(3,924,124)
Total accumulated depreciation	(24,964,693)	-	(2,344,503)	(27,309,196)
Total capital assets being depreciated, net	53,584,670	5,604,835	(2,344,503)	56,845,002
Governmental activities capital assets, net	\$ 60,163,872	\$ 9,673,645	\$ (2,344,503)	\$ 67,493,014
Depreciation expense was charged to functions/programs as follows:				
General government	\$ 158,015			
Public safety	326,561			
Education	1,429,982			
Public works	121,578			
Health and human services	107,172			
Culture and recreation	201,195			
	\$ 2,344,503			

## CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002III. Detailed Notes to All Funds (continued)

## D. Capital Assets (continued)

	Beginning Balance	Increases	Decreases	Ending Balance
<u>Business Activities:</u>				
Capital assets not being depreciated:				
Land	\$ 276,422	\$ -	\$ -	\$ 276,422
Capital assets being depreciated:				
Buildings and improvements	8,084,513			8,084,513
Improvement other than buildings	437,660			437,660
Machinery and equipment	218,844			218,844
Vehicles	136,154			136,154
Total capital assets being depreciated	8,877,171	-	-	8,877,171
Less accumulated depreciation for:				
Buildings and improvements	(2,427,786)		(201,361)	(2,628,609)
Improvement other than buildings	(245,729)		(13,989)	(259,718)
Machinery and equipment	(189,989)		(6,254)	(196,243)
Vehicles	(136,154)			(136,154)
Total accumulated depreciation	(2,999,658)	-	(221,604)	(3,220,724)
Total capital assets being depreciated, net	5,877,513	-	(221,604)	5,656,447
Business activities capital assets, net	<u>\$ 6,153,935</u>	<u>\$ -</u>	<u>\$ (221,604)</u>	<u>\$ 5,932,869</u>
Depreciation expense was charged to functions/programs as follows:				
Water and sewer	\$ 2,999			
Golf course	28,112			
Parking activities	190,493			
	<u>\$ 221,604</u>			

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

III. Detailed Notes to All Funds (continued)

E. Leases

Lessee Agreements – The following significant capital leases relate to the City acting as the lessee. These leases are primarily attributable to vehicles and equipment of the Public Works, Cemetery, and Fire Departments, and the remainder is for computer leases associated with the School Department future payments on leases consist of the following:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
June 30,			
2003	\$ 706,559	\$ 65,832	\$ 772,391
2004	112,666	22,829	135,495
2005	89,710	16,230	105,940
2006	94,823	11,117	105,940
2007	100,228	5,712	105,940
Thereafter	<u>0</u>	<u>0</u>	<u>0</u>
Totals	<u>\$ 1,103,986</u>	<u>\$ 121,720</u>	<u>\$ 1,225,706</u>

F. Temporary Debt

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

Current Operating Costs – Prior to the collection of revenues, expenditures may be financed through the issuance of revenue or tax anticipation notes (RANS or TANS).

Capital Projects and Other Approved Costs – Projects may be temporarily funded through the issuance of bond anticipation notes (BANS) or grant anticipation notes (GANS). In certain cases, prior to the issuance of these temporary notes, the governing body must take the necessary legal steps to authorize the issuance of the general obligation bonds. Temporary notes may not exceed the aggregate amount of bonds authorized or the grant award amount.

Temporary notes are general obligations of the City and carry maturity dates not in excess of one year and are interest bearing and will be paid through future issuance of general obligation bonds. Temporary notes outstanding at June 30, 2002, recorded in the Governmental Funds are payable as follows:

<u>Project</u>	<u>Type</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Amount</u>
School construction	BAN	2.25%	1/16/03	\$ 30,000,000
School construction	BAN	2.25%	1/16/03	<u>5,646,000</u>
				<u>\$ 35,646,000</u>

Subsequent to the balance sheet date, \$21,146,000 of the temporary notes were refinanced as long-term bonds as part of a \$28,670,000 bond issuance by the City, accordingly, they have been reflected as long-term liabilities in the Statement of Net Assets.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

III. Other Information (continued)

G. Long-Term Debt

The City issues general obligation bonds and notes to provide funds for the acquisition and construction of major capital facilities. General obligation bonds and notes have been issued for both governmental and business-type activities. Additionally, the City incurs various other long-term obligations relative to associated personnel costs. During the year ended June 30, 2002, the following reflects the activity in the long-term liability accounts:

	Balance July 1, 2001	Additions	Reductions	Balance June 30, 2002
<i>Governmental Activities:</i>				
Notes payable	\$ 965,000		\$ ( 85,000)	\$ 880,000
Capital leases	1,929,115		( 825,129)	1,103,986
Compensated absences	3,845,450			3,845,450
Risk financing	369,009	\$ 8,827,068	( 8,725,228)	470,849
Bond indebtedness	40,230,000	-	( 2,605,000)	37,625,000
Total Governmental	<u>\$ 47,338,574</u>	<u>\$ 8,827,068</u>	<u>\$ (12,240,357)</u>	<u>\$ 43,925,285</u>
<i>Business-type Activities:</i>				
Bond indebtedness	\$ 850,000	\$ -	\$ ( 200,000)	\$ 650,000
Total Business-type	<u>\$ 850,000</u>	<u>\$ -</u>	<u>\$ ( 200,000)</u>	<u>\$ 650,000</u>

See footnote F. Temporary notes refinanced to Bonds subsequent to the balance sheet date have been reflected as long-term liabilities on the Statement of Net Assets. The Bonds are payable over 20 years and bear interest at 3 to 5%.

Legal Debt Margin – State law permits a city, under the provisions of Chapter 44, Section 10, to authorize indebtedness up to a limit of 2.5% of its equalized valuation. Debt issued in accordance with this section of the law is designated as being “inside the debt limit.” In addition, a City may authorize debt in excess of that limit for specific purposes. Such debt, when issued, is designated as being “outside the debt limit.” The following is a computation of the legal debt margin as of June 30, 2002 (in thousands of dollars):

Equalized Valuation –		
Real Estate and Personal Property		<u>\$ 2,858,057</u>
Debt Limit – 2 ½% of Equalized Valuation		71,451
Total Debt (including authorized and unissued)	\$ 122,188	
Less: Debt exempt from Limit	( 116,563)	<u>( 5,625)</u>
Legal Debt Margin		<u>\$ 65,826</u>



## CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002III. Detailed Notes to All Funds (continued)

## G. Long-Term Debt

Bond Debt Issued - The following is a summary of outstanding long-term debt obligations for the year ended June 30, 2002:

Description of Issue	Year of Issue	Maturity Date	Interest Rate	Original Amounts	Amounts Outstanding
<i>Governmental Activities:</i>					
Inside the debt limit:					
Police Station	01/15/94	01/15/04	4.15 - 5.25%	\$ 200,000	\$ 40,000
School Renovation	07/01/96	08/15/15	5.125 - 5.75%	1,800,000	1,310,000
Swimming Pool	09/15/00	06/30/17	4.50 - 6.75%	450,000	405,000
Computer Hardware & Software	09/15/00	06/30/03	6.75%	990,000	495,000
Police Station	08/01/01	07/15/11	3.50 - 4.00%	2,935,000	2,935,000
Total inside the debt limit					5,185,000
Outside the debt limit:					
School Construction	01/15/94	01/15/13	4.15 - 5.25%	9,000,000	5,200,000
School Remodeling	07/01/96	08/15/15	5.125 - 5.75%	7,000,000	5,640,000
School Construction	09/15/00	06/30/20	4.50 - 6.75%	10,705,000	10,395,000
School Construction	08/01/01	07/15/11	3.50 - 4.00%	6,495,000	6,495,000
School Construction	08/01/01	07/15/11	3.50 - 4.00%	4,710,000	4,710,000
Total outside the debt limit					32,440,000
<b>Total Governmental Activities</b>					<b>\$ 37,625,000</b>
<i>Business-type Activities:</i>					
Inside the debt limit:					
Golf Course	09/15/00	06/30/17	4.50 - 6.75%	470,000	\$ 440,000
Total inside the debt limit					440,000
Outside the debt limit:					
Water	01/15/94	01/15/04	4.15 - 5.25%	1,050,000	210,000
Total outside the debt limit					210,000
<b>Total Business-type Activities</b>					<b>\$ 650,000</b>

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

III. Detailed Notes to All Funds (continued)

G. Long-Term Debt (continued)

Future Debt Payoff - Payments on general long-term debt obligation bonds due in future years consist of the following:

Year Ending June 30	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2003	\$ 2,795,000	\$ 1,959,172	\$ 135,000	\$ 27,748
2004	2,945,000	1,569,233	135,000	21,349
2005	2,960,000	1,438,553	30,000	17,563
2006	2,980,000	1,306,822	30,000	16,175
2007	3,005,000	1,174,427	30,000	14,825
Thereafter	22,940,000	5,273,648	290,000	69,025
Total	<u>\$ 37,625,000</u>	<u>\$ 12,721,855</u>	<u>\$ 650,000</u>	<u>\$ 166,685</u>

Authorized and Unissued Debt - At June 30, 2002, the City had authorized and unissued debt as follows:

Project	Amount
School Construction (outside debt)	\$ 83,033,130
Total authorized and unissued	<u>\$ 83,033,130</u>

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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III. Detailed Notes on All Funds (continued)

G. Long-Term Debt (continued)

Notes Payable -

1. On June 29, 1989, the City borrowed \$600,000 from the Federal Housing and Urban Development Department (HUD) under the Section 108 CDBG program. Upon its maturity date of August 1, 1999, the City renegotiated the loan with HUD for \$540,000 after an initial up-front payment of \$60,000 and extended the maturity date to August 1, 2009. The City's future entitlements of community development block grants have been pledged as security for repayments of this loan. Principal payments are due annually commencing on August 1, 2000. Interest is due in quarterly payments at a rate of LIBOR + .2% on the unpaid principal beginning on August 1, 1999. As of June 30, 2002, \$430,000 remained outstanding.

2. On February 1, 1995, the City, borrowed a total of \$600,000 from HUD under Section 108 CDBG Program. This loan package consists of 8 separate promissory notes at \$55,000 and one at \$60,000, aggregating \$500,000, guaranteed by HUD. The notes are secured by future City entitlement of community development block grants funds. Principal payments are due annually commencing on August 1, 1997, and ending August 1, 2014. Beginning August 1, 1995, interest is payable semi-annually on February 1 and August 1 at a rate of 9.0%. As of June 30, 2002, \$450,000 remained outstanding.

Maturities on these notes at June 30, 2002 are as follows:

Year Ending June 30	Governmental Activities	
	Principal	Interest*
2003	\$ 85,000	\$ 37,668
2004	90,000	34,984
2005	90,000	32,095
2006	90,000	29,185
2007	90,000	26,234
Thereafter	435,000	99,935
Total	<u>\$ 880,000</u>	<u>\$ 260,101</u>

\* This amount does not include the variable interest due annually on the first note described above. For the year ended June 30, 2002, the actual interest paid on the note was \$14,200.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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III. Detailed Notes on All Funds (continued)

G. Long-Term Debt (continued)

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 approximated below (unaudited):

<u>Related Entity</u>	<u>Principal (thousands)</u>	<u>Percent</u>	<u>Amount (thousands)</u>
North Shore Regional Vocational	\$ 3,460	24.70%	\$ 855
MBTA	3,757,145	.74%	27,803
South Essex Sewerage District	190,374	19.99%	38,056
			<u>\$ 66,714</u>

IV. Other Information

A. Retirement System

System Description – The City contributes to the City of Salem Contributory Retirement System (the System), an agency multiple-employer defined benefit pension plan for the City, Salem Housing Authority, Salem and Beverly Water Board, South Essex Sewerage District, and North Shore Regional Vocational School. The System was established under Chapter 32 of the General Laws of the Commonwealth of Massachusetts. The System is administered by the City of Salem and is part of the reporting entity. A stand-alone financial report for the year ended December 31, 2001, was issued and is available at the Retirement Office, 93 Washington Street, Salem, Massachusetts.

Substantially all employees of the City, except teachers and certain administrative personnel employed by the School Department, participate in the System. The members of the System do not participate in the Social Security System. Benefits paid under the System, 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 payroll for employees covered by the System for the year ended December 31, 2001, was approximately \$29,072,000.

Teachers and certain administrative employees of the School Department participate in a contributory retirement system administered by the Massachusetts Teachers Retirement Board. Contributions to that system totaled \$4,275,669 the year and were made entirely by the Commonwealth of Massachusetts, on behalf of the City, which does not contribute directly to this system.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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IV. Other Information (continued)

A. Retirement System (continued)

Membership – Current membership in the System as of December 31, 2001, is as follows:

Retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them	599
Active employees	909
Inactive employees	<u>98</u>
Total	<u>1,606</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 portions of the interest they generate constitute the annuity. The differential between the total retirement benefit and annuity is the pension.

From time to time, the Legislature may grant cost-of-living increases to benefits being paid to retirees. These increases are 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 participating units. These units are responsible for the full cost-of-living 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 granted to retirees prior to 1998 for the duration of their 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 0%, 50% or 100% of the regular interest that 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.

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.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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IV. Other Information (continued)

A. Retirement System (continued)

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.

Contribution Requirements and Contributions Made – The System'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 System 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.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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IV. Other Information (continued)

A. Retirement System (continued)

Investment Concentration – There were no investments (other than those issued or guaranteed by the United States Government) in any one organization that represents 5% or more of the System's net assets.

Disclosures – Required disclosures under Governmental Accounting Standards Board's Statements No. 25 and 27 are included in this report under the caption "Required Supplementary Information".

- B. **Risk Financing** – The City has established a self-insured medical program which is accounted for in the Health Claims Trust Fund in the Governmental Funds Permanent Fund. Both employees and the City contribute to the payment of medical claims based upon a 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 Governmental Funds Permanent 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, 2002.

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.

Activity regarding this account for the year ended June 30, 2002 is as follows:

Liability at beginning of year	\$ 369,009
Provision for losses	8,827,068
Payments for claims	( 8,725,228)
Liability at end of year	<u>\$ 470,849</u>

Disclosures – Required disclosures under Governmental Accounting Standards Board's Statements No. 25 and 27 are included in this report under the caption "Required Supplementary Information".

- C. **Post Employment Benefits** – In addition to providing pension benefits, the City provides the majority of retired employees with payments for a portion of their health care and life insurance benefits. These benefits are provided through various health maintenance organizations. Benefits paid by the City are on a pay-as-you-go basis. There is no actuarial valuation available as of June 30, 2002, which would permit an estimation of the unfunded past service cost liability, future costs of current participants in the system and annual amounts needed to fund such costs. The cost to fund these benefits amounted to approximately \$800,000 for each of the last three fiscal years.

CITY OF SALEM, MASSACHUSETTS

NOTES TO BASIC FINANCIAL STATEMENTS - CONTINUED  
YEAR ENDED JUNE 30, 2002

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IV. Other Information (continued)

- D. **Contingencies** – The City is party to certain legal claims, which are subject to many uncertainties, and the outcome of individual litigation matters is not always predictable with assurance. Although the amount of liability, if any, at June 30, 2002, cannot be ascertained, management believes that any resulting liability, if any, should not materially affect the basic financial statements of the City at June 30, 2002.

Amounts received or receivable from grantor agencies are subject to audit and adjustment by grantor agencies, principally the federal and state governments. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, 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.

The City is subject to certain Federal arbitrage laws in accordance with long-term borrowing agreements. 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.

IV. Certain Segment Information

The following segment information is provided for the Water and Sewer Business-type activities not including joint venture information:

	<u>Water</u>	<u>Sewer</u>	<u>Total</u>
Revenues	\$3,483,728	\$6,311,164	\$9,794,892
Operating Expenses	(3,677,484)	(7,165,335)	(10,842,819)
Interest expense	( 13,650)		( 13,650)
Transfers in (out), net	20,225		20,225
Indirect costs paid to General Fund	<u>( 693,618)</u>	<u>( 693,618)</u>	<u>1,387,236</u>
Net income (deficit)	( 880,799)	(1,547,789)	(2,428,588)
Net assets, July 1, 2001	<u>2,646,311</u>	<u>2,694,622</u>	<u>5,340,933</u>
Net assets, June 30, 2002	<u>\$1,765,512</u>	<u>\$1,146,833</u>	<u>\$2,912,345</u>



CITY OF SALEM, MASSACHUSETTS

REQUIRED SUPPLEMENTARY INFORMATION - RETIREMENT SYSTEM  
YEAR ENDED DECEMBER 31, 2001

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a/c)
01/01/01	\$73,727,923	\$117,334,727	\$43,606,804	62.8%	\$29,072,197	150%
01/01/99	68,563,143	111,294,953	42,731,810	61.6%	25,411,629	168%
01/01/97	51,236,360	82,440,774	31,204,414	62.1%	22,930,939	136%
01/01/94	41,074,617	71,831,709	30,757,092	57.2%	17,753,129	173%
01/01/92	33,180,956	76,039,158	42,858,202	43.6%	16,993,481	252%

Schedule of Contributions Made by Employers

Year Ended December 31,	Annual Required Contribution	Percentage Contributed
2001	\$4,610,788	100%
2000	4,452,134	100%
1999	4,410,289	100%
1998	4,268,352	100%
1997	4,003,864	100%
1996	3,943,853	100%
1995	3,887,240	100%
1994	4,347,948	100%
1993	5,233,797	100%
1992	5,091,808	100%

Notes to Schedules

Additional information as of the latest actuarial valuation follows:

Valuation date:	January 1, 2001
Actuarial cost method:	Individual entry age normal
Amortization method:	Required payments increase of 4.5% per year
Remaining amortization period:	27 years
Asset valuation method:	Fair Value
Investment rate of return:	8.5%
Projected salary increases:	5.5%
Cost-of-living adjustments	3.0% of the lessor of the pension amount and \$12,000 per year