

CITY OF ROCHESTER, NEW HAMPSHIRE
Financial Statements
With Schedule of Expenditures of Federal Awards
June 30, 2006
and
Independent Auditor's Opinion

**Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of
Financial Statements Performed in Accordance With
*Government Auditing Standards***

**Report on Compliance With Requirements Applicable
to Each Major Program and Internal Control Over
Compliance in Accordance With OMB Circular A-133**

Schedule of Findings and Questioned Costs

CITY OF ROCHESTER, NEW HAMPSHIRE
FINANCIAL STATEMENTS
June 30, 2006

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FINANCIAL STATEMENTS
June 30, 2006

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INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor, City Council and Manager
City of Rochester, New Hampshire

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund, and the aggregate remaining fund information of the City of Rochester, New Hampshire (The City) as of and for the year ended June 30, 2006, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business type activities, each major fund, and the aggregate remaining fund information of the City as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2006 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis and the Required Supplementary Information on pages i-viii and 30-31, respectively, are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods

of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City of Rochester's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects, in relation to the basic financial statements taken as a whole.

Wachon, Chukay & Co., PC

October 25, 2006

City of Rochester, New Hampshire

Management's Discussion and Analysis

Our discussion and analysis of the City of Rochester's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2006. Please read this analysis in conjunction with the transmittal letter and financial statements presented in this report.

These financial reports represent the fourth year the City of Rochester has implemented the new Governmental Accounting Standards Board Statement No. 34 (GASB 34). This fourth year is building on the statistics for a more meaningful trend and explanation of the City's finances and changes in financial position.

FINANCIAL HIGHLIGHTS

Government-wide Highlights

- The City's total assets, \$125.1 million, exceeded total liabilities, \$73.1 million, by \$52.0 million. This amount is the Total Net Assets on Exhibit A, Statement of Net Assets for Governmental Activities. The \$52.0 million is reported as \$39.5 million invested in capital assets, net of related debt, \$6.7 million restricted and \$5.8 million in unrestricted funds. The unrestricted balance represents the amount available to be used to meet the City's ongoing obligations to citizens and creditors.
- The City's net assets increased by \$2.2 million or 2% in fiscal year 2006. The change in assets for Governmental Activities increased by \$1.4 million or 2% and Business-type Activities increased by \$.8 million or 2%.

Fund Highlights

- The Fund Balance for all governmental funds increased by \$8.9 million to \$14.1 million for fiscal year ending June 30, 2006. This amount is the Fund Balances at end of year on Exhibit D, Statement of Revenues, Expenditures and Changes in Fund Balances. The General Fund Balance increased by \$1.7 million to \$7.3 million. The fund balance for all other funds increased by \$7.2 million to \$6.7 million.
- Total cost of all of the City's programs, not including grants, donations and capital projects, increased by \$4.5 million or 7.0%.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities (Exhibits A, B, C and D) present information about the activities of the City as a whole and present a longer-term view of the City's finances. Fund financial statements are presented in Exhibits E, F and G. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's most significant funds. The remaining statements provide financial information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

Reporting the City as a Whole

Our analysis of the City as a whole begins with Exhibit A. One of the most important questions asked about the City's finances is: "Is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Activities report information about the City as a whole and about its activities in a way that helps answer this question. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting method used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the City's *net* assets and changes in them. The City's net assets can be thought of as the **difference** between assets and liabilities, as one way to measure the City's financial health, or *financial position*. Over time, increases *or* decreases in the City's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the City's property tax base and the condition of the City's roads, to assess the *overall health* of the City.

The Statement of Net Assets and the Statement of Activities is divided into two kinds of activities:

- **Governmental activities** - Most of the City's basic services are reported here, including the police, fire, public works, parks and recreation, and general administration. Property taxes, franchise fees, and state and federal grants finance most of these activities.
- **Business-type activities** - The City charges a fee to customers to help it cover all or most of the cost of certain services the City provides. The City's Water, Sewer, and Arena Funds are reported here.

Reporting the City's Most Significant Funds

Our analysis of the City's major funds begins with Exhibit B, Statement of Activities. These financial statements provide detailed information about the most significant funds - not the City as a whole. Some funds are required to be established by State law and by bond covenants. However, the City Council establishes many other funds to help it control and manage money for particular purposes, (e.g. capital improvements, school food service program, Community Center operations, major grants and other business-type activities) or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money (like grants received from the state or federal government). The City's two kinds of funds- *governmental* and *proprietary* - use different accounting approaches.

- **Governmental funds** - Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the year-end balances that are available for spending. These funds are reported using an accounting method called *modified accrual* accounting, which measures cash and all other *financial* assets that can readily be converted to cash. The governmental fund statements provide a detailed *short-term view* of the City's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. We describe the relationship (or differences) between governmental *activities* (reported in the Statement of Net Assets and the Statement of Activities) and governmental *funds* in reconciliation at the end of the fund financial statements.
- **Proprietary funds** - When the City charges customers for the services it provides - whether to outside customers or to other units of the City. These services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the City's enterprise funds (a component of proprietary funds) are the same as the business-type activities (Water, Sewer and Arena) reported in the government-wide statements but provide more detail and additional information, such as cash flows for proprietary funds.
- **The City as Trustee**

The City is the trustee, or *fiduciary*, for its employees' 457 and 403(b) pension plans. It is also responsible for other assets that, because of a trust arrangement, can be used only for the trust beneficiaries (Library Trust, School Trusts and Cemetery Trusts). All of the City's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets on Exhibits H and I. These activities are excluded from the City's other financial statements because the City cannot use these assets to finance its operations. The City is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

THE CITY AS A WHOLE

The City's *combined* total net assets are \$92.5 million. Separating the net assets and net expenses of Governmental and Business-type Activities, this represents \$52.0 million for Governmental Activities and \$40.5 million for Business-type Activities.

Table 1
Net Assets
(in Millions)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2006	2005	2006	2005	2006	2005
Current and other assets	36.0	26.1	5.3	9.4	41.3	35.6
Capital assets	<u>89.1</u>	<u>82.7</u>	<u>63.7</u>	<u>60.0</u>	<u>152.8</u>	<u>142.7</u>
Total Assets	125.1	108.8	69.0	69.4	194.1	178.3
Long-term debt outstanding	(45.4)	(33.5)	(23.9)	(25.3)	(69.3)	(58.8)
Other liabilities	<u>(27.7)</u>	<u>(25.0)</u>	<u>(4.6)</u>	<u>(4.4)</u>	<u>(32.3)</u>	<u>(29.4)</u>
Total liabilities	(73.1)	(58.5)	(28.5)	(29.7)	(101.6)	(88.2)
Invested in capital assets, net of debt	39.5	46.7	36.6	31.5	76.1	78.2
Restricted	6.7	(3.2)	-	-	6.7	(3.2)
Unrestricted (deficit)	<u>5.8</u>	<u>6.8</u>	<u>3.9</u>	<u>8.2</u>	<u>9.7</u>	<u>15.0</u>
Total net assets	52.0	50.3	40.5	39.7	92.5	90.0

The largest portion of the City's net assets is investments in land, buildings, equipment and infrastructure less any outstanding debt.

The City's unrestricted governmental net assets decreased by \$1.0 million to \$5.8 million. This decrease does not represent an unanticipated negative change in the City's overall fiscal health. The decrease in unrestricted net assets is almost entirely due to the difference between construction in progress and the bond sale in December of 2005. The City's ability to complete major capital projects with cash on hand prior to the actual sale of the bonds to finance the projects, is a testament to its strong fiscal health. The strength of the City is also due to its fiscally conservative practices in past years. It is incumbent on the City to maintain these practices to remain financially sound.

The net assets of the City's business-type activities are investments in the water and sewer plants, related infrastructure, and the arena building/equipment. These funds however, cannot be used to make up for the other governmental activities. The City generally can only use these net assets to finance the continuing operations of the Water, Sewer and Arena.

The City's net assets increased by \$2.2 million, as presented in Table 2 below. The largest expenditures are from Education, Public Safety, Public Works and General Government. The difference in funding between expenses and revenues is made up through property taxes.

Changes in Net Assets
(in Millions)

	Governmental Activities		Business-type Activities		Total Primary Activities	
	2006	2005	2006	2005	2006	2005
Revenues						
Program revenues:						
Charges for services	2.3	2.2	7.1	6.6	9.4	8.8
Federal Grants	25.0	21.2	-	-	25.0	21.2
State grants and entitlements	0.1	0.4	-	-	0.1	0.4
General Revenues:						
Property taxes	38.4	37.1	-	-	38.4	37.1
Other taxes	4.8	4.7	-	-	4.8	4.7
Federal entitlements	-	-	-	-	-	-
Other general revenues	<u>6.4</u>	<u>5.9</u>	<u>0.4</u>	<u>0.4</u>	<u>6.8</u>	<u>6.3</u>
Total revenues	77.0	71.5	7.5	7.0	84.5	78.5
Program Expenses						
General government	3.4	3.2	-	-	3.4	3.2
Public safety	9.3	9.0	-	-	9.3	9.0
Public works	5.9	5.7	-	-	5.9	5.7
Health and welfare	0.8	0.7	-	-	0.8	0.7
Culture and recreation	1.5	1.5	-	-	1.5	1.5
Community development	0.5	0.7	-	-	0.5	0.7
Community services	0.6	0.5	-	-	0.6	0.5
Education	45.4	42.8	-	-	45.4	42.8
Food services	1.6	1.5	-	-	1.6	1.5
Capital outlay	-	0.1	-	-	-	0.1
Interest on long-term debt	2.1	1.9	-	-	2.1	1.9
Intergovernmental	4.4	3.5	-	-	4.4	3.5
Water	-	-	2.5	2.2	2.5	2.2
Sewer	-	-	3.9	3.6	3.9	3.6
Arena	<u>-</u>	<u>-</u>	<u>0.4</u>	<u>0.4</u>	<u>0.4</u>	<u>0.4</u>
Total Expenses	75.5	71.1	6.8	6.2	82.3	77.3
Excess (deficiency) before special items and transfers	1.5	0.4	0.7	0.8	2.2	1.2
Transfers	<u>-</u>	<u>(0.2)</u>	<u>-</u>	<u>0.2</u>	<u>-</u>	<u>-</u>
Increase (decrease) in net assets	1.5	0.2	0.7	1.0	2.2	1.2

Governmental Activities

The City recognizes that maintaining a strong financial position is crucial to the City's long-term success. The burden that is placed on citizens and businesses must be taken into consideration with all financial decisions. The major fiscal challenges facing the City are: level or decreased State funding for education, health insurance increases, State retirement increases, energy costs, property values and tax rates. Fortunately, other City/School revenues have exceeded expectations and conservative spending has produced balances in many accounts at the end

Governmental Activities

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- The City's assessed property value for taxation increased to \$2.23 billion or 23.0% increase as of April 1, 2005. Of the valuation increase, approximately \$41.0 million was due to new construction. The tax rate decreased to \$17.30 or 15.0% over the previous year.
- The City is committed to infrastructure and capital improvements. The capital budget for fiscal year 2006 was \$22.3 million. Of this amount \$11.2 million was earmarked for the School Department's energy upgrade program of which nearly 60% will be reimbursed from the New Hampshire Department of Education School Building Aid program. Of the remaining \$11.1 million almost 80% was specifically earmarked for Highway, Water and Sewer improvements. Other major projects include Fire Department apparatus replacement and other school facilities upgrades

The major areas where revenues exceeded projections are taxes: \$257 thousand; licenses and permits, \$174 thousand; interest income, \$495 thousand and miscellaneous revenues, \$136 thousand. Additional budget to actual variances can be found on Schedule 1, Statement of Revenues, Expenditures and Changes in Fund Balances. Although the national economy has weakened during fiscal year 2006, the New Hampshire economy has not faltered substantially. The housing market has flattened, sales of existing homes have slowed and the double digit increases of real estate values have stopped. Additionally, the domestic auto manufacturers are experiencing significant challenges and the purchase of ever more expensive automobiles is slowing. The good news is that energy prices have stabilized and in most cases have decreased and employment remains strong.

Here in Rochester, even though the City is recognizing a slowdown in more expensive auto registrations, a substantial reduction in overall auto registration has not occurred up to this point, unlike other Southern New Hampshire communities. While construction of single family homes has weakened, construction of commercial buildings is expected to remain strong to moderate through the remainder of calendar year 2007. The conservatism that Rochester has embraced over the years must remain one of the keys to the City's continued financial strength.

Business-type Activities

Operating revenues for the City's business-type activities exceeded expenses by \$764 thousand as presented in Exhibit F of the attached statements.

- The City sewer system posted a change in net assets of \$160 thousand. Although a loss was anticipated for this year, conservative fiscal management and increases in charges for services have helped this fund considerably. Cash flow is also a major concern for this fund with respect to servicing the debt for the new plant. Exhibit G, Statement of Cash Flows Proprietary Funds, reports a \$1.5 million decrease in cash balance from the beginning of the year. While this is not a positive change from the previous years, continued evaluation of the cash flow needs and expected rate changes is essential to the sound management of this fund. The actions taken by the City in the past few years are a thorough review of Sewer Fund revenues and expenses and recommendations for annual rate increases to continue positive cash flow in future years.
- The City water system has produced an operating profit for several years and with the expiration of several bond issues in the next few years the fund is anticipated to remain profitable in the near future. Cash flow in the Water Fund as reported in Exhibit G is also being reviewed in conjunction with the Sewer Fund rate reviews. However, some increases in the water rate will be necessary to maintain positive operations.
- The City Ice Arena has a reported net asset change of \$(12) thousand. The current loss in this fund is also due

to the interest on the debt service of the construction/improvements to the arena. While this loss was also anticipated, the operating loss trend has decreased and it is anticipated that the Arena will start producing an operating profit in the next few years. The actions taken by the City are continued increases in ice time rental rates and a restructuring of the City's Recreation and Arena departments to consolidate management and realize savings in wages and benefits. It is important to keep a critical eye on trends and market conditions for this fund.

- The negative cash balances in the Business-type Activities operations is not unexpected and is a direct result of completing capital projects before bonding takes place. The City's overall cash balance is strong and is able to accommodate the cash flow fluctuations in the proprietary funds.

THE CITY'S FUNDS

As the City completed the year, its Governmental Funds as presented in the Statement of Revenues, Expenditures and Changes in Fund Balances on Schedule 1, reported a budgetary fund balance of \$7.9 million, which is ahead of last year's total of \$5.9 million. Included in this year's total change in Fund Balance, however, is the budgeted use of \$950 thousand from Fund Balance to decrease the amount of dollars needed to raise in taxes, less the actual excess revenues and over (under) expenditures.

General Fund Budgetary Highlights

Over the course of the year, the City Council revised the City General Fund-operating budget twice. Supplemental appropriations were passed to increase the Public Works Department's Hot Top Cold Patch line by \$65,800 and the Transfer to Conservation Commission line by \$247,932. Total expenditure budget increase was \$313,732; the total offsetting revenue budget increase was \$247,932 from excess Current Use Tax Penalties and \$65,800 thousand was funded from surplus.

Additional supplemental appropriations were approved by the City Council at various other times throughout the year for grants and donations for several City departments.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The City's investment in capital assets for its Governmental and Business-type Activities as of June 30, 2006 is \$279.3 million (see Table 3 below). Accumulated depreciation amounts to \$126.5 million, leaving a Total Capital Assets net balance of \$152.8 million. This investment in capital assets includes land, buildings, equipment, computer software, construction in progress and infrastructure. Infrastructure assets are items that are normally immovable, of value only to the City and include roads and bridges. GASB Statement No. 34 requires assets, including infrastructure, for the City's governmental funds reported in the General Fixed Asset Account Group. This is the second year fixed assets are reported in compliance with the new GASB requirements

Table 3
Capital Assets at Year-end
(net of Depreciation, in Millions)

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Land	6.8	5.7	2.2	2.2	9.0	7.9
Land improvements	3.8	3.5	-	-	3.8	3.5
Buildings & improvements	49.0	48.6	43.4	43.6	92.4	92.2
Vehicles & equipment	9.6	8.8	3.7	2.7	13.3	11.5
Infrastructure	112.9	109.9	32.6	29.5	145.5	139.4
Construction in progress	<u>10.5</u>	<u>4.6</u>	<u>4.8</u>	<u>3.3</u>	<u>15.3</u>	<u>7.9</u>
Totals	192.6	181.1	86.7	81.3	279.3	262.4

Debt

The City may issue general obligation bonds, receive State Revolving Fund notes in lieu of bonds, and notes in anticipation of such bonds, taxes and other anticipated revenues. Although the City does issue general obligation bonds regularly and receives State Revolving Loan Funds, it has been many years since the issuance of any anticipation notes. As of June 30, 2006, the total debt outstanding for all funds is \$76.6 million. See Table 4 below.

Table 4
Outstanding Debt at Year-end
(in Millions)

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
General obligation bonds (backed by the City) and State revolving notes	<u>49.5</u>	<u>36.1</u>	<u>27.1</u>	<u>28.5</u>	<u>76.6</u>	<u>64.6</u>
Totals	49.5	36.1	27.1	28.5	76.6	64.6

The City's overall debt limitations and available debt margin are listed in Note 8 – General Obligation Debt, of the Financial Statements

The City's general obligation bond rating remains at A3. While financial steadfastness is only one of the criteria that bond rating agencies use in assessing overall risk, continued positive performance in this area will help lead the City to continued increases in bond ratings which in turn mean lower rates and savings to taxpayers.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's elected and appointed officials considered many factors when setting the fiscal year 2007 budget and the resulting impact on tax rates, bills and the fees that will be charged for business-type activities. One of those factors

is the economy. As of June 30, 2006, the New Hampshire Employment Security Economic and Labor Market Information Bureau reported that unemployment in the City stands at 3.2 % versus 3.4% a year ago. This compares favorably with the State's unemployment rate of 3.3 % and the national rate of 4.8 %. At the same time, the need for welfare assistance by working families continues to increase.

The City understands that it needs to provide an excellent infrastructure and have a proactive recruitment and retention program in order to create additional employment opportunities, attract new businesses, and expand existing businesses. The City continues to take steps in that direction for the fiscal year 2007 in both the operating and capital budgets. The Economic Development Manager is producing excellent results in business retention and new development initiatives. Several high profile developments have broken ground, a major shopping center including Kohl's and Lowe's as anchor tenants, expansion of an existing Wal-mart to a superstore, a new Hannaford grocery store (already open), a Harley Davidson dealership and other commercial developments along the major highway corridors of the City.

Of the \$15.5 million approved for capital improvements, approximately \$14 million will focus on infrastructure items namely road improvements and upgrades to water and sewer delivery/collection systems. The balance, nearly \$1.5 million is being invested in School Department upgrades, Arena upgrades, Public Buildings, technology and various other programs.

While it is important to the City Council and the community to provide appropriate levels of service to taxpayers, diversify the tax base, and create new investment in the City, it is equally important to maintain financial stability and equitable taxation. The City has many resources at its disposal that make it a very attractive community within which to live and work. As mentioned earlier, several high profile commercial development projects have already begun. Rochester also has industrial property available for development, continuously improving infrastructure, the newest sewer treatment plant in the seacoast region, desirable housing for a range of socioeconomic groups, an expanding state of the art hospital, a high-tech landfill, excellent schools, and it is centrally located near the region's most attractive natural resources. It is anticipated that new commercial/industrial development will increase employment opportunities and continue to expand the current tax base.

There are many volunteer groups in the community that work to bring others to Rochester. Among the most active groups are the Rochester Economic Development Commission, the Rochester Main Street Program (formerly the Community Organization for Rochester Enhancement), the Lilac City Fun Festival Committee and the Greater Rochester Chamber of Commerce. One of Rochester's prized charms is the Historic Rochester Opera House located on the second floor of City Hall. It is nearly 100 years old and is one of the oldest, restored, and the only remaining opera house with functioning moving floors in the United States. Taken together, these factors provide the foundation and framework necessary to maintain and expand Rochester's reputation as a desirable and financially stable City.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the City Finance Office at 31 Wakefield Street, Rochester, NH 03867.

EXHIBIT A
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Net Assets
June 30, 2006

	Primary Government		
	Governmental	Business-type	
	<u>Activities</u>	<u>Activities</u>	<u>Total</u>
ASSETS			
Current Assets:			
Cash and cash equivalents	\$ 7,793,403		\$ 7,793,403
Investments	22,644,660		22,644,660
Taxes receivable, net	893,305		893,305
Accounts receivable, net	1,640,937	\$ 1,790,328	3,431,265
Due from other governments	1,387,637	4,800,509	6,188,146
Internal balances	1,511,060	(1,511,060)	-
Prepaid expenses	12,191	13,793	25,984
Inventory	19,617	204,366	223,983
Tax dedeed property	122,279		122,279
Total Current Assets	<u>36,025,089</u>	<u>5,297,936</u>	<u>41,323,025</u>
Noncurrent Assets:			
Non-depreciable capital assets	17,258,001	6,999,247	24,257,248
Depreciable capital assets, net	<u>71,780,631</u>	<u>56,661,242</u>	<u>128,441,873</u>
Total Noncurrent Assets	<u>89,038,632</u>	<u>63,660,489</u>	<u>152,699,121</u>
Total Assets	<u>\$ 125,063,721</u>	<u>\$ 68,958,425</u>	<u>\$ 194,022,146</u>
LIABILITIES			
Current Liabilities:			
Accounts payable	\$ 2,291,581	\$ 132,736	\$ 2,424,317
Accrued expenses	4,754,131	924,437	5,678,568
Retainage payable	336,438	334,816	671,254
Deposits	406,527	1,732	408,259
Deferred revenue	14,582,607	5,000	14,587,607
Deferred bond premium	187,089		187,089
Current portion of bonds payable	<u>5,143,725</u>	<u>3,193,557</u>	<u>8,337,282</u>
Total Current Liabilities	<u>27,702,098</u>	<u>4,592,278</u>	<u>32,294,376</u>
Noncurrent Liabilities:			
Bonds payable	44,396,442		44,396,442
Notes payable		23,900,779	23,900,779
Compensated absences	<u>967,116</u>		<u>967,116</u>
Total Noncurrent Liabilities	<u>45,363,558</u>	<u>23,900,779</u>	<u>69,264,337</u>
Total Liabilities	<u>73,065,656</u>	<u>28,493,057</u>	<u>101,558,713</u>
NET ASSETS			
Invested in capital assets, net of related debt	39,498,465	36,566,153	76,064,618
Restricted	6,696,527		6,696,527
Unrestricted	<u>5,803,073</u>	<u>3,899,215</u>	<u>9,702,288</u>
Total Net Assets	<u>51,998,065</u>	<u>40,465,368</u>	<u>92,463,433</u>
Total Net Assets and Liabilities	<u>\$ 125,063,721</u>	<u>\$ 68,958,425</u>	<u>\$ 194,022,146</u>

See accompanying notes to the basic financial statements

EXHIBIT B
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Activities
For the Year Ended June 30, 2006

Functions/Programs	<u>Expenses</u>	<u>Program Revenues</u>			<u>Net (Expense) Revenue and Changes in Net Assets</u>		
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	<u>Primary Government</u>		<u>Total</u>
					<u>Governmental Activities</u>	<u>Business-type Activities</u>	
Governmental Activities:							
General government	\$ 3,431,072	\$ 172,986	\$ -	\$ -	\$ (3,258,086)		\$ (3,258,086)
Public safety	9,334,924	284,945	382,008	12,136	(8,655,835)		(8,655,835)
Highways and streets	5,857,612	89,109	498,635	-	(5,269,868)		(5,269,868)
Health and welfare	788,158		-	-	(788,158)		(788,158)
Culture and recreation	1,517,800	140,178	-	-	(1,377,622)		(1,377,622)
Community development	509,480		252,147		(257,333)		(257,333)
Community services	605,787	570,879			(34,908)		(34,908)
Education	45,392,550	168,573	23,196,106		(22,027,871)		(22,027,871)
Food service	1,572,691	888,540	654,697		(29,454)		(29,454)
Capital outlay	38,963			31,618	(7,345)		(7,345)
Interest and fiscal charges	2,070,062				(2,070,062)		(2,070,062)
Intergovernmental	4,379,097				(4,379,097)		(4,379,097)
Total governmental activities	<u>75,498,196</u>	<u>2,315,210</u>	<u>24,983,593</u>	<u>43,754</u>	<u>(48,155,639)</u>	<u>\$ -</u>	<u>(48,155,639)</u>
Business-type activities:							
Sewer	3,849,919	3,801,484				(48,435)	(48,435)
Water	2,466,213	2,879,848				413,635	413,635
Arena	417,789	404,519				(13,270)	(13,270)
Total business-type activities	<u>6,733,921</u>	<u>7,085,851</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>351,930</u>	<u>351,930</u>
Total primary government	<u>\$ 82,232,117</u>	<u>\$ 9,401,061</u>	<u>\$ 24,983,593</u>	<u>\$ 43,754</u>	<u>(48,155,639)</u>	<u>351,930</u>	<u>(47,803,709)</u>
General revenues:							
Property taxes					38,421,656		38,421,656
Licenses and permits					4,793,221		4,793,221
Intergovernmental revenue					1,621,618		1,621,618
Interest and investment earnings					872,593	217,994	1,090,587
Miscellaneous					3,883,643	18,066	3,901,709
Capital contributions						176,324	176,324
Total general revenues and transfers					<u>49,592,731</u>	<u>412,384</u>	<u>50,005,115</u>
Change in net assets					1,437,092	764,314	2,201,406
Net assets - beginning - (as restated)					50,560,973	39,701,054	90,262,027
Net assets - ending					<u>\$ 51,998,065</u>	<u>\$ 40,465,368</u>	<u>\$ 92,463,433</u>

See accompanying notes to the basic financial statements

EXHIBIT C
CITY OF ROCHESTER, NEW HAMPSHIRE
Balance Sheet
Governmental Funds
June 30, 2006

	General <u>Fund</u>	Capital Projects <u>Fund</u>	Other Governmental <u>Funds</u>	Total Governmental <u>Funds</u>
ASSETS				
Cash and cash equivalents	\$ 7,621,681		\$ 171,722	\$ 7,793,403
Investments	22,593,445		51,215	22,644,660
Taxes receivable, net	893,305			893,305
Accounts receivable, net	1,176,498		464,439	1,640,937
Due from other governments		\$ 310,003	1,077,634	1,387,637
Due from other funds	5,356,136	4,293,070	3,166,668	12,815,874
Prepaid expenses	12,191			12,191
Inventory	3,244		16,373	19,617
Tax dedeed property	122,279			122,279
Total Assets	<u>\$ 37,778,779</u>	<u>\$ 4,603,073</u>	<u>\$ 4,948,051</u>	<u>\$ 47,329,903</u>
LIABILITIES				
Accounts payable	\$ 1,332,185	\$ 707,730	\$ 251,666	\$ 2,291,581
Accrued expenses	3,750,510		12,468	3,762,978
Retainage payable		336,438	-	336,438
Deposits	406,527			406,527
Deferred revenue	14,756,519	25,760	390,156	15,172,435
Due to other funds	10,203,692		1,101,122	11,304,814
Total Liabilities	<u>30,449,433</u>	<u>1,069,928</u>	<u>1,755,412</u>	<u>33,274,773</u>
FUND BALANCES				
Reserved for endowments			38,331	38,331
Reserved for prepaid expenses	12,191			12,191
Reserved for inventory	3,244		16,373	19,617
Reserved for special purposes	20,000			20,000
Unreserved reported in:				
General fund	7,293,911			7,293,911
Special revenue funds			3,125,051	3,125,051
Capital projects funds		3,533,145	-	3,533,145
Permanent funds			12,884	12,884
Total Fund Balances	<u>7,329,346</u>	<u>3,533,145</u>	<u>3,192,639</u>	<u>14,055,130</u>
Total Liabilities and Fund Balances	<u>\$ 37,778,779</u>	<u>\$ 4,603,073</u>	<u>\$ 4,948,051</u>	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	89,038,632
Property taxes are recognized on an accrual basis in the statement of net assets, not the modified accrual basis	589,828
Deferred debt expense is recognized on an accrual basis in the statement of net assets, not the modified accrual basis	(187,089)
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds. Long-term liabilities at year end consist of:	
Bonds payable	(49,540,167)
Compensated absences	(967,116)
Accrued interest on long-term obligations	(991,153)

Net assets of governmental activities	<u>\$ 51,998,065</u>
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See accompanying notes to the basic financial statements

EXHIBIT D

CITY OF ROCHESTER, NEW HAMPSHIRE

Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds

For the Year Ended June 30, 2006

	General Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Revenues:				
Taxes	\$ 38,140,208			\$ 38,140,208
Licenses and permits	4,793,221			4,793,221
Intergovernmental	22,194,740	\$ 31,618	\$ 4,422,607	26,648,965
Charges for services	680,489		1,634,721	2,315,210
Interest income	870,238		2,355	872,593
Miscellaneous	2,717,430	1,034,687	131,526	3,883,643
Total Revenues	<u>69,396,326</u>	<u>1,066,305</u>	<u>6,191,209</u>	<u>76,653,840</u>
Expenditures:				
Current operations:				
General government	3,176,383		794	3,177,177
Public safety	9,036,942		106,933	9,143,875
Highways and streets	2,220,418			2,220,418
Health and welfare	788,185			788,185
Culture and recreation	1,463,474		4,457	1,467,931
Community development	97,193		412,287	509,480
Community services			604,599	604,599
Education	40,832,882		3,601,661	44,434,543
Food service			1,565,632	1,565,632
Capital outlay		11,419,361		11,419,361
Debt service:				
Principal retirement	3,668,948			3,668,948
Interest and fiscal charges	1,742,558			1,742,558
Intergovernmental	4,379,097			4,379,097
Total Expenditures	<u>67,406,080</u>	<u>11,419,361</u>	<u>6,296,363</u>	<u>85,121,804</u>
Excess of revenues over (under) expenditures	<u>1,990,246</u>	<u>(10,353,056)</u>	<u>(105,154)</u>	<u>(8,467,964)</u>
Other financing sources (uses):				
Proceeds from issuance of debt		17,335,843		17,335,843
Operating transfers in	365,057	386,000	602,940	1,353,997
Operating transfers out	(585,082)	(610,415)	(158,500)	(1,353,997)
Total other financing sources (uses)	<u>(220,025)</u>	<u>17,111,428</u>	<u>444,440</u>	<u>17,335,843</u>
Excess of revenues and other sources under expenditures and other uses	<u>1,770,221</u>	<u>6,758,372</u>	<u>339,286</u>	<u>8,867,879</u>
Fund balances (Deficit) at beginning of year, as restated	<u>5,559,125</u>	<u>(3,225,227)</u>	<u>2,853,353</u>	<u>5,187,251</u>
Fund balances at end of year	<u>\$ 7,329,346</u>	<u>\$ 3,533,145</u>	<u>\$ 3,192,639</u>	<u>\$ 14,055,130</u>

See accompanying notes to the basic financial statements

CITY OF ROCHESTER, NEW HAMPSHIRE

Reconciliation of the Statement of Revenues, Expenditures
and Changes in Fund Balances of Governmental Funds
to the Statement of Activities

For the Year Ended June 30, 2006

New Change in Fund Balances--Total Governmental Funds	\$ 8,867,879
Amounts reported for governmental activities in the statement of activities are different because:	
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 as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	6,293,743
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	281,448
Proceeds from bond issues are an other financing source in the funds, but a bond issue increases long-term liabilities in the statement of net assets.	(17,335,843)
Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.	3,668,948
In the statement of activities, interest is accrued on outstanding bonds, whereas in governmental funds, an interest expenditure is reported when due.	(327,504)
Some expense reported in the statement of activities, such as compensated absences, do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.	(11,579)
Change in Net Assets of Governmental Activities	<u>\$ 1,437,092</u>

EXHIBIT E
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Net Assets
Proprietary Funds
June 30, 2006

	Business-type Activities			
	<u>Sewer Fund</u>	<u>Water Fund</u>	<u>Arena Fund</u>	<u>Totals</u>
ASSETS				
Current Assets:				
Accounts receivable, net	\$ 959,550	\$ 830,778		\$ 1,790,328
Due from other governments	4,726,097	74,412		4,800,509
Due from other funds	1,928,911	763,236	\$ 59,426	2,751,573
Prepaid expenses		13,793		13,793
Inventory		204,366		204,366
Total Current Assets	<u>7,614,558</u>	<u>1,886,585</u>	<u>59,426</u>	<u>9,560,569</u>
Noncurrent Assets:				
Non-depreciable capital assets	4,111,978	2,815,296	71,973	6,999,247
Depreciable capital assets, net	38,406,879	17,180,109	1,074,254	56,661,242
Total Noncurrent Assets	<u>42,518,857</u>	<u>19,995,405</u>	<u>1,146,227</u>	<u>63,660,489</u>
Total Assets	<u>\$ 50,133,415</u>	<u>\$ 21,881,990</u>	<u>\$ 1,205,653</u>	<u>\$ 73,221,058</u>
LIABILITIES				
Current Liabilities:				
Accounts payable	\$ 70,503	\$ 58,204	\$ 4,029	\$ 132,736
Accrued expenses	715,250	180,537	28,650	924,437
Retainage payable	181,622	153,194		334,816
Deferred revenue			1,732	1,732
Deposits		5,000		5,000
Due to other funds	2,187,413	2,075,220		4,262,633
Current portion of notes payable	1,570,329	1,565,992	57,236	3,193,557
Total Current Liabilities	<u>4,725,117</u>	<u>4,038,147</u>	<u>91,647</u>	<u>8,854,911</u>
Noncurrent Liabilities:				
Notes payable	19,612,035	3,358,627	930,117	23,900,779
Total Noncurrent Liabilities	<u>19,612,035</u>	<u>3,358,627</u>	<u>930,117</u>	<u>23,900,779</u>
Total Liabilities	<u>24,337,152</u>	<u>7,396,774</u>	<u>1,021,764</u>	<u>32,755,690</u>
NET ASSETS				
Invested in capital assets, net of related debt	21,336,493	15,070,786	158,874	36,566,153
Unrestricted (Deficit)	4,459,770	(585,570)	25,015	3,899,215
Total Net Assets	<u>25,796,263</u>	<u>14,485,216</u>	<u>183,889</u>	<u>40,465,368</u>
Total Liabilities and Net Assets	<u>\$ 50,133,415</u>	<u>\$ 21,881,990</u>	<u>\$ 1,205,653</u>	<u>\$ 73,221,058</u>

See accompanying notes to the basic financial statements

EXHIBIT F

CITY OF ROCHESTER, NEW HAMPSHIRE

Statement of Revenues, Expenses and Changes in Net Assets

Proprietary Funds

For the Year Ended June 30, 2006

	Business-type Activities			
	Sewer Fund	Water Fund	Arena Fund	Totals
Operating revenues:				
Charges for services	\$ 3,801,484	\$ 2,879,848	\$ 404,519	\$ 7,085,851
Miscellaneous	3,889	14,139	38	18,066
Total operating revenues	<u>3,805,373</u>	<u>2,893,987</u>	<u>404,557</u>	<u>7,103,917</u>
Operating expenses:				
Personal services	831,262	966,802	175,805	1,973,869
Materials and supplies	313,390	277,561	10,478	601,429
Utilities	683,811	109,620	99,852	893,283
Depreciation	912,302	669,745	43,501	1,625,548
Miscellaneous	224,327	257,549	42,431	524,307
Total operating expenses	<u>2,965,092</u>	<u>2,281,277</u>	<u>372,067</u>	<u>5,618,436</u>
Operating income	<u>840,281</u>	<u>612,710</u>	<u>32,490</u>	<u>1,485,481</u>
Non-operating revenues (expenses):				
Interest revenue	198,750	17,994	1,250	217,994
Interest expense	(884,827)	(184,936)	(45,722)	(1,115,485)
Net non-operating revenues (expenses)	<u>(686,077)</u>	<u>(166,942)</u>	<u>(44,472)</u>	<u>(897,491)</u>
Income (Loss) before contributions and transfers	154,204	445,768	(11,982)	587,990
Capital contributions	<u>5,584</u>	<u>170,740</u>		<u>176,324</u>
Change in net assets	159,788	616,508	(11,982)	764,314
Total net assets at beginning of year	<u>25,636,475</u>	<u>13,868,708</u>	<u>195,871</u>	<u>39,701,054</u>
Total net assets at end of year	<u>\$ 25,796,263</u>	<u>\$ 14,485,216</u>	<u>\$ 183,889</u>	<u>\$ 40,465,368</u>

See accompanying notes to the basic financial statements

EXHIBIT G
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Cash Flows
Proprietary Funds
For the Year Ended June 30, 2006

	Business-type Activities			
	<u>Sewer Fund</u>	<u>Water Fund</u>	<u>Arena Fund</u>	<u>Totals</u>
Cash flows from operating activities:				
Cash received from customers	\$ 4,045,585	\$ 3,493,521	\$ 407,540	\$ 7,946,646
Cash paid to suppliers and employees	(2,017,111)	(1,621,206)	(321,401)	(3,959,718)
Net cash provided by operating activities	<u>2,028,474</u>	<u>1,872,315</u>	<u>86,139</u>	<u>3,986,928</u>
Cash flows from capital and related financing activities:				
Purchases of capital assets	(2,258,566)	(2,890,383)		(5,148,949)
Proceeds of note payable	1,083,858	577,669		1,661,527
Principal paid on note payable	(1,660,584)	(1,511,457)	(57,235)	(3,229,276)
Interest paid on note payable	(898,990)	(187,125)	(46,670)	(1,132,785)
Capital contributions	5,584	160,000	-	165,584
Net cash used for capital and related financing activities	<u>(3,728,698)</u>	<u>(3,851,296)</u>	<u>(103,905)</u>	<u>(7,683,899)</u>
Cash flows from investing activities:				
Interest on investments	198,750	17,994	1,250	217,994
Net cash provided by investing activities	<u>198,750</u>	<u>17,994</u>	<u>1,250</u>	<u>217,994</u>
Net (decrease) in cash and cash equivalents	(1,501,474)	(1,960,987)	(16,516)	(3,478,977)
Cash and cash equivalents at beginning of year	1,242,972	649,003	75,942	1,967,917
Cash and cash equivalents at end of year	<u>\$ (258,502)</u>	<u>\$ (1,311,984)</u>	<u>\$ 59,426</u>	<u>\$ (1,511,060)</u>
Reconciliation of operating income to net cash provided by operating activities:				
Operating income	\$ 840,281	\$ 612,710	\$ 32,490	\$ 1,485,481
Adjustments to reconcile operating loss to net cash provided by operating activities:				
Depreciation expense	912,302	669,745	43,501	1,625,548
Changes in assets and liabilities:				
Accounts receivable, net	(78,763)	(73,186)	3,288	(148,661)
Due from other governments	318,975	679,675		998,650
Prepaid expenses	-	8,827	-	8,827
Inventory		(34,142)		(34,142)
Accounts payable	27,155	(5,637)	572	22,090
Accrued expenses	8,524	16,278	6,593	31,395
Deferred revenue		(6,955)	(305)	(7,260)
Deposits		5,000		5,000
Net cash provided by operating activities	<u>\$ 2,028,474</u>	<u>\$ 1,872,315</u>	<u>\$ 86,139</u>	<u>\$ 3,986,928</u>

See accompanying notes to the basic financial statements

EXHIBIT H
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Fiduciary Net Assets
Fiduciary Funds
June 30, 2006

	Private- Purpose <u>Trusts</u>	Agency <u>Funds</u>
ASSETS		
Cash and cash equivalents	\$ 21,154	\$ 202,337
Investments	<u>1,091,762</u>	
Total assets	<u>\$ 1,112,916</u>	<u>\$ 202,337</u>
LIABILITIES		
Due to student groups		<u>\$ 202,337</u>
Total liabilities	<u>\$ -</u>	<u>\$ 202,337</u>
NET ASSETS		
Held in trust	<u>1,112,916</u>	
Total net assets	<u>\$ 1,112,916</u>	

See accompanying notes to the basic financial statements

EXHIBIT I
CITY OF ROCHESTER, NEW HAMPSHIRE
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
For the Year Ended June 30, 2006

	Private- Purpose <u>Trust Fund</u>
ADDITIONS:	
Contributions:	
Private donations	\$ 2,822
Total Contributions	<u>2,822</u>
Investment earnings:	
Interest	70,832
Net decrease in the fair value of investments	<u>(26,965)</u>
Total Investment Earnings	<u>43,867</u>
Less investment expense	<u>-</u>
Net Investment Earnings	<u>43,867</u>
Total Additions	<u>46,689</u>
DEDUCTIONS:	
Benefits	<u>27,253</u>
Total Deductions	<u>27,253</u>
Change in Net Assets	19,436
Net assets - beginning of year	<u>1,093,480</u>
Net assets - end of year	<u>\$ 1,112,916</u>

See accompanying notes to the basic financial statements

**CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS
For the Year Ended June 30, 2006**

NOTE 1--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Rochester, New Hampshire conform to accounting policies generally accepted in the United States of America for local governmental units, except as indicated hereinafter. The following is a summary of significant accounting policies.

Financial Reporting Entity

The government is a municipal corporation governed by an elected City Council. The City operates under the Mayor/City Council/Manager form of government and performs local governmental functions as authorized by its charter.

The accompanying financial statements of the City present the financial position of the various fund types and account groups, the results of operations of the various fund types, and the cash flows of the proprietary fund types and similar trust funds types.

As required by accounting principles generally accepted in the United States of America, these financial statements present the government and applicable component units for which the government is considered to be financially accountable. In fiscal year 2006, it was determined that no entities met the required GASB-14 criteria of component units.

Basis of Presentation

The City's basic financial statements consist of government-wide statements, including a statement of net assets and a statement of activities, and fund financial statements which provide a more detailed level of financial information.

1. Government-Wide Financial Statements:

The statement of net assets and the statement of activities display information about the City as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The statement of net assets presents the financial condition of the governmental activities of the City at year end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the City's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program, grants and contributions that are restricted to meeting the operational or capital requirements of a particular program and interest earned on grants that is required to be used to support a particular program. Revenues which are not classified as program revenues are presented as general revenues of the City. The comparison of direct expenses with program revenues identifies the extent to which each governmental function is self-financing or draws from the general revenues of the City.

2. Fund Financial Statements:

During the year, the City segregates transactions related to certain City functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

statements are designed to present financial information of the City at this more detailed level. The focus of governmental fund financial statements is on major funds. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. The fiduciary funds are reported by type.

Fund Accounting

The City uses funds to maintain its financial records during the fiscal year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. There are three categories of funds: governmental, proprietary and fiduciary.

1. Governmental Funds:

Governmental funds are those through which most governmental functions typically are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following are the City's major governmental funds:

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

The Capital Projects Fund accounts for all financial resources to be used for the acquisition or construction of major capital facilities and equipment (other than those financed by proprietary funds).

Other non-major governmental funds consist of the following special revenue funds: Community Development Fund, Police Grants Fund, Miscellaneous grants fund, other school grants fund, Homeland Security Grants fund, Food Service Fund, Federal Projects Fund, Economic Development Fund, Planning Fund, Conservation Commission Fund, and Rochester Community Center Fund. All of these funds have similar characteristics in which the revenues are restricted in nature for specific expenditures.

2. Proprietary Funds:

Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position and cash flows. Proprietary funds are classified as enterprise or internal service. The City has no internal service funds. The following are the City's major proprietary funds:

The Sewer Fund accounts for all revenues and expenses pertaining to the City's sanitation operations.

The Water Fund accounts for all revenues and expenses pertaining to the City's water operations.

The Arena Fund accounts for all revenues and expenses pertaining to the City's ice arena operations.

The Sewer, Water and Arena Funds are utilized to account for operations that are financed and operated in a manner similar to private business enterprises. The stated intent is that the cost (i.e. expenses including depreciation) of providing goods or services to the residents on a continuing basis are financed or recovered primarily through user charges.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

3. Fiduciary Funds:

Fiduciary fund reporting focuses on net assets and changes in net assets. The fiduciary fund category is split into two classifications: private purpose trust funds, and agency funds. Trust funds are used to account for assets held by the City under a trust agreement for individuals, private organizations, or other governments and are therefore not available to support the City's own programs. The City maintains four private purpose trusts which account for monies designated to benefit individuals within the City. The City's agency fund is custodial in nature (assets equal liabilities) and does not involve the measurement of results of operations. The City's agency fund accounts for Student Activities Funds of the school.

Measurement Focus

1. Government-Wide Financial Statements:

The government-wide financial statements are prepared using the economic resources measurement focus. All assets and liabilities associated with the operation of the City are included on the Statement of Net Assets.

2. Fund Financial Statements:

All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. The statement of revenues, expenditures and changes in fund balances reports on the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activities of the government-wide financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

Like the government-wide statements, the proprietary fund type is accounted for on a flow of economic resources measurement focus. All assets and all liabilities associated with the operation of these funds are included on the statement of net assets. The statement of changes in fund net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The statement of cash flows provides information about how the City finances and meets the cash flow needs of its proprietary activities.

The private purpose trust fund is reported using the economic resources measurement focus.

Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Proprietary and fiduciary funds also use the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Differences in the accrual and the modified accrual basis of accounting arise in the recognition of revenue, the recording of deferred revenue, and in the presentation of expenses versus expenditures.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

In the government-wide financial statements and proprietary fund statements, private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

1. Revenues – Exchange and Non-exchange Transactions:

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the City, available means expected to be received within sixty days of fiscal year end.

Non-exchange transactions, in which the City receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied (see Note 2). Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted; matching requirements, in which the City must provide local resources to be used for a specified purpose; and expenditure requirements, in which the resources are provided to the City on a reimbursement basis. On a modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Under the modified accrual basis, the following revenue sources are considered to be both measurable and available at fiscal year end: property taxes and interest on investments.

Licenses and permits, charges for services, and miscellaneous revenues (except interest on investments) are recorded as revenues when received in cash because they are generally not measurable until actually received.

2. Deferred Revenue:

Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied. Grants and entitlements received before the eligibility requirements are met are recorded as deferred revenue. On governmental fund financial statements, receivables that will not be collected within the available period have also been reported as deferred revenue.

3. Expenses/Expenditures:

On the accrual basis of accounting, expenses are recognized at the time they are incurred.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation and amortization are not recognized in governmental funds.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Budgetary Data

The City's budget represents functional appropriations as authorized by annual or special Council meetings. The Council may transfer funds between operating categories as they deem necessary. The City adopts its budget under State regulations, which differ somewhat from accounting principles generally accepted in the United States of America in that the focus is on the entire governmental unit rather than on the basis of fund types.

State law requires balanced budgets but permits the use of beginning fund balance to reduce the property tax rate. For the year ended June 30, 2006, the City applied \$687,583 of its unappropriated fund balance to reduce taxes.

Cash and Cash Equivalents

The City pools its cash resources for the governmental and proprietary funds. Cash applicable to a particular fund is reflected as an interfund balance. For the purpose of the Statement of Cash Flows, cash and cash equivalents consist of the following:

	Interfund Receivable/ (Payable)
Proprietary Funds:	
Sewer Fund	\$ (258,502)
Water Fund	(1,311,984)
Nonmajor Fund	59,426
	<u>\$ (1,511,060)</u>

Investments

Investments are stated at their fair value in all funds. Certificates of deposit and repurchase agreements with a maturity of greater than ninety days from the date of issuance are included in investments.

Taxes Receivable

Taxes levied during the current fiscal year and prior and uncollected at June 30, 2006 are recorded as receivables net of reserves for estimated uncollectibles of \$3,417,641.

Prepaid Expenses

Payments made to vendors for services that will benefit periods beyond June 30, 2006 are recorded as prepaid items.

Inventory

The City accounts for inventories under the purchase method on a first-in, first out basis. Inventories are recorded at cost.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Capital Assets

General capital assets result from expenditures in the governmental and proprietary funds. These assets are reported in the government-wide statement of net assets, but are not reported in the fund financial statements. All capital assets including infrastructure are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. The City maintains a capitalization threshold of \$10,000. The City's infrastructure consists of roads, bridges, sidewalks, water purification and distribution system, sewer collection and treatment system, and similar items. Improvements are capitalized; the costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not. Interest incurred during the construction of capital assets is also capitalized.

All reported capital assets except for land and construction in progress are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Useful lives for infrastructure were estimated based on the City's historical records of necessary improvements and replacement. Depreciation is computed using the straight-line method over the following useful lives:

The City capitalizes interest costs during a project's construction period.

<u>Description</u>	<u>Years</u>
Infrastructure	10 - 50
Structures and Land improvements	10 - 50
Mains, Pump Stations, and Sewer Lines	40 - 100
Equipment	3 - 100
Waster Water Treatment Plant	50
Furniture and Fixtures	7

Compensated Absences

City employees are granted vacation and sick leave in varying amounts. Upon retirement, termination, or death, certain employees are compensated for unused sick and vacation leave which is (subject to certain limitations) at their then current rates of pay. The estimated cost of unused sick and vacation leave which may be payable upon retirement or termination has been recorded in the government-wide financial statements.

Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities, and long-term obligations are reported in the government-wide financial statements. In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current resources, are reported as obligations of the funds. However, compensated absences that will be paid from governmental funds are reported as liabilities in the fund financial statements only to the extent that they are due for payment during the current fiscal year. General obligation bonds and other long-term obligations that will be paid from governmental funds are recognized as a liability in the fund financial statements when due.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances on any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The City's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Fund Balance Reserves

The City reserves those portions of fund balance which are legally segregated for a specific future use or which do not represent available expendable resources and, therefore, are not available for appropriation or expenditure. Unreserved fund balance indicates that portion which is available for appropriation in future periods.

Interfund Activity

Transfers between governmental and business-type activities on the government-wide statements are reported in the same manner as general revenues.

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and after non-operating revenues/expenses in the proprietary funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the water fund and sewer fund, these revenues are charges to customers for sales and services. Operating expenses, which include depreciation on capital assets, are necessary costs incurred to provide the service that is the primary activity of the proprietary fund. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America require management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

NOTE 2--PROPERTY TAXES

Taxes are levied on the assessed valuation of all taxable real property as of the prior April 1 (\$2,231,365,655 as of April 1, 2005) and are due in two installments on December 17, 2005 and July 2, 2005. Taxes paid after the due dates accrue interest at 12% per annum. Property taxes are recognized as revenue when received in cash or if available to finance current period operations (within sixty days of year end).

Under State law, the Tax Collector obtains tax liens on properties which have unpaid taxes in the following calendar year after taxes were due for the amount of unpaid taxes, interest and costs. These priority tax liens accrue interest at 18% per annum. If the property is not redeemed within a two year redemption period, the property is tax deeded to the City.

In accordance with State law, the City collects taxes for Strafford County, an independent governmental unit, which are remitted to the County as required by law. Total taxes appropriated to Strafford County for the year ended June 30, 2006 were \$4,379,097. The City bears responsibility for uncollected taxes.

NOTE 3--RISK MANAGEMENT

The City is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the year ended June 30, 2006, the City was a member of the Local Government Center Property-Liability Insurance Trust, Inc. (LGC-PLIT) and the New Hampshire Public Risk Management Exchange (PRIMEX). The City currently reports all of its risk management activities in its General Fund. These Trusts are classified as a "Risk Pools" in accordance with accounting principles generally accepted in the United States of America.

The Trust agreements permit the Trusts to make additional assessments to members should there be a deficiency in Trust assets to meet its liabilities. Accounting principles generally accepted in the United States of America require members of pools with a sharing of risk to determine whether or not such assessment is probable and, if so, a reasonable estimate of such assessment. At this time, the Trusts foresee no likelihood of an additional assessment for any of the past years. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. Based on the best available information there is no liability at June 30, 2006.

Property and Liability Insurance

The LGC-PLIT provides certain property and liability insurance coverage to member towns, cities, and other qualified political subdivisions of New Hampshire. As a member of the LGC-PLIT, the City shares in contributing to the cost of and receiving benefit from a self-insured pooled risk management program. The program includes a Self Insured Retention Fund from which is paid up to \$500,000 for each and every covered property, crime and/or liability loss that exceeds \$1,000.

Worker's Compensation

PRIMEX provides statutory worker's compensation coverage to member towns, cities, and other qualified political subdivisions of New Hampshire. The Trust is self-sustaining through annual member premiums and provides coverage for the statutorily required workers' compensation benefits and employer's

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

liability coverage up to \$2,000,000. The program includes a Loss Fund from which is paid up to \$500,000 for each and every covered claim.

NOTE 4--CASH AND INVESTMENTS

Cash and investments as of June 30, 2006 are classified in the accompanying financial statements as follows:

Statement of net assets:	
Cash and cash equivalents	\$ 7,793,403
Investments	22,644,660
Statement of fiduciary net assets:	
Cash and cash equivalents	223,491
Investments	1,091,762
Total cash and investments	<u>\$ 31,753,316</u>

Cash and investments as of June 30, 2006 consist of the following:

Cash on hand	\$ 7,656
Deposits with financial institutions	30,592,633
Investments	1,153,027
Total cash and investments	<u>\$ 31,753,316</u>

The City has combined the cash resources of its governmental fund types and business-type activities. For accounting and reporting purposes, that portion of the pooled cash balance is reported in the specific fund as an interfund balances.

The City's investment policy for governmental fund types requires that deposits and investments be made in New Hampshire based financial institutions that are participants in one of the federal depository insurance programs. The City limits its investments to demand deposits, money market accounts, certificates of deposit, and repurchase agreements in accordance with New Hampshire State law (RSA 41:29) or the New Hampshire Public Deposit Investment Pool (NHPDIP), an external investment pool. Responsibility for the investments of the Trust Funds is with the Board of Trustees.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the City manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time.

Information about the sensitivity of the fair values of the City's investments to market interest rate fluctuations is provided by the following table that shows the distribution of investments by maturity:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

<u>Investment Type</u>		<u>Remaining Maturity (in Years)</u>		
		<u>0-1 Years</u>	<u>1-5 Years</u>	<u>More Than 5 Years</u>
Federal agency securities	\$ 179,073	\$ 35,131	\$ 77,460	\$ 66,482
U.S. Treasury Notes	25,082	25,082		
Corporate bonds	242,883	49,466	84,396	109,021
	<u>\$ 447,038</u>	<u>\$ 109,679</u>	<u>\$ 161,856</u>	<u>\$ 175,503</u>

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The following is the actual rating as of year end for each investment type.

<u>Investment Type</u>		<u>Rating as of Year End</u>						<u>Not Rated</u>
		<u>AAA</u>	<u>AA</u>	<u>A1</u>	<u>A3</u>	<u>AA1</u>	<u>AA3</u>	
Federal agency securities	\$ 179,073	\$ 179,073						
Corporate bonds	242,883	29,424	\$ 28,757	\$ 87,839	\$ 25,022	\$ 24,996	\$ 46,845	
Equity securities	513,401							\$ 513,401
State investment pool	10,049							10,049
Mutual funds	55,826							55,826
	<u>\$ 1,001,232</u>	<u>\$ 208,497</u>	<u>\$ 28,757</u>	<u>\$ 87,839</u>	<u>\$ 25,022</u>	<u>\$ 24,996</u>	<u>\$ 46,845</u>	<u>\$ 579,276</u>

Custodial Credit Risk

Custodial credit risk for deposits is the risk that in the event of a bank failure, the City's deposits may not be returned to it. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party.

Of the City's deposits with financial institutions at year end \$33,708,634 was collateralized by securities held by the bank in the bank's name. As of June 30, 2006, District investments in the following investment types were held by the same counterparty that was used to buy the securities.

<u>Investment Type</u>	<u>Reported Amount</u>
Equity securities	\$ 513,401
Corporate bonds	242,883
Money market mutual funds	182,539
	<u>\$ 938,823</u>

Investment in NHPDIP

The City is a voluntary participant in the New Hampshire Public Deposit Pool (NHPDIP). The NHPDIP is not registered with the United States Securities and Exchange Commission as an investment company.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

The NHPDIP was created by state law and is administered by a public body of state, local and banking officials.

Investments in the NHPDIP are not investment securities and, as such, are not categorized by risk. The City's exposure to derivatives is indirect through its participation in the NHPDIP. The City's proportional share of these derivatives is not available. The fair value of the position in the investment pool is equal to the value of the pool shares.

NOTE 5--DUE FROM OTHER GOVERNMENTS

Receivables from other governments at June 30, 2006 consists of various federal and state reimbursement receivables. All receivables are considered collectible in full and will be received within one year. A summary of the principal items of intergovernmental receivables is as follows:

State of New Hampshire - Bridge Aid	\$ 77,769
State of New Hampshire	232,234
Community Development Block grant	12,569
Police grants	33,153
Homeland Security grant	2,099
Food service reimbursement	47,090
State and federal school grant reimbursements	982,723
State filtration grant	4,726,097
Sewer state aid grant reimbursement	74,412
	<u>\$ 6,188,146</u>

NOTE 6--CAPITAL ASSETS AND DEPRECIATION

The following is a summary of changes in capital assets in the governmental funds:

	<u>Balance</u> <u>7/1/2005</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>6/30/2006</u>
Governmental activities:				
Capital asset not depreciated:				
Land	\$ 5,703,100	\$ 1,037,476		\$ 6,740,576
Construction in process	4,643,824	11,380,399	\$(5,506,798)	10,517,425
Total capital assets not being depreciated	<u>10,346,924</u>	<u>12,417,875</u>	<u>(5,506,798)</u>	<u>17,258,001</u>
Other capital assets:				
Infrastructure	109,856,786	3,067,953		112,924,739
Land improvements	3,510,347	323,195		3,833,542
Buildings and improvements	48,585,399	359,737		48,945,136
Vehicles and equipment	8,812,743	808,103		9,620,846
Total other capital assets at historical cost	<u>170,765,275</u>	<u>4,558,988</u>	<u>-</u>	<u>175,324,263</u>

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Less accumulated depreciation for:

Infrastructure	(76,043,406)	(3,463,640)		(79,507,046)
Land improvements	(1,721,032)	(166,179)		(1,887,211)
Buildings and improvements	(15,191,837)	(929,143)		(16,120,980)
Vehicles and equipment	(5,411,035)	(617,360)		(6,028,395)
Total accumulated depreciation	<u>(98,367,310)</u>	<u>(5,176,322)</u>	<u>-</u>	<u>(103,543,632)</u>
Total other capital assets, net	<u>72,397,965</u>	<u>(617,334)</u>	<u>-</u>	<u>71,780,631</u>
Total capital assets, net	<u>\$ 82,744,889</u>	<u>\$ 11,800,541</u>	<u>\$(5,506,798)</u>	<u>\$ 89,038,632</u>

Depreciation was charged to functions as follows:

General government	\$ 260,347
Public safety	313,551
Highways and streets	3,637,057
Culture and recreation	51,801
Community services	1,188
Education	906,422
Food service	5,956
Total governmental activities depreciation expense	<u>\$ 5,176,322</u>

The following is a summary of changes in capital assets in the proprietary funds:

	Balance 7/1/2005	Additions	Reductions	Balance 6/30/2006
Business-type activities:				
Capital asset not depreciated:				
Land	\$ 2,221,430			\$ 2,221,430
Construction in process	<u>3,314,403</u>	<u>\$ 3,757,198</u>	<u>\$(2,293,784)</u>	<u>4,777,817</u>
Total capital assets not being depreciated	<u>5,535,833</u>	<u>3,757,198</u>	<u>(2,293,784)</u>	<u>6,999,247</u>
Other capital assets:				
Infrastructure	29,480,352	3,163,951		32,644,303
Buildings and improvements	43,343,044	17,728		43,360,772
Vehicles and equipment	<u>2,983,624</u>	<u>665,280</u>		<u>3,648,904</u>
Total other capital assets at historical cost	<u>75,807,020</u>	<u>3,846,959</u>	<u>-</u>	<u>79,653,979</u>
Less accumulated depreciation for:				
Infrastructure	(8,758,112)	(568,535)		(9,326,647)
Buildings and improvements	(10,868,051)	(885,042)		(11,753,093)
Vehicles and equipment	<u>(1,741,026)</u>	<u>(171,971)</u>		<u>(1,912,997)</u>
Total accumulated depreciation	<u>(21,367,189)</u>	<u>(1,625,548)</u>	<u>-</u>	<u>(22,992,737)</u>
Total other capital assets, net	<u>54,439,831</u>	<u>2,221,411</u>	<u>-</u>	<u>56,661,242</u>
Total capital assets, net	<u>\$ 59,975,664</u>	<u>\$ 5,978,609</u>	<u>\$(2,293,784)</u>	<u>\$ 63,660,489</u>

Depreciation was charged to proprietary funds as follows:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Sewer fund	\$ 912,302
Water fund	669,745
Arena fund	<u>43,501</u>
Total business-type activities depreciation expense	<u>\$ 1,625,548</u>

NOTE 7--DEFINED BENEFIT PENSION PLAN

Plan Description

The City contributes to the New Hampshire Retirement System (NHRS), a cost-sharing, multiple-employer, defined benefit pension plan administrated by the NHRS Board of Trustees. The plan provides service, disability, death and vested retirement allowances to plan members and beneficiaries. Benefit provisions are established and may be amended by the New Hampshire State legislature. The NHRS issues a publicly available financial report that includes financial statements and required supplementary information for NHRS. That report can be obtained by writing to New Hampshire Retirement System at 4 Chenell Drive, Concord, New Hampshire 03301-8509.

Funding Policy

Covered public safety employees are required to contribute 9.3% of their covered salary, whereas teachers and general employees are required to contribute 5.0% of their covered salary. The City is required to contribute at an actuarially determined rate. The City's contribution rates for the covered payroll of police officers, fire employees, teachers, and general employees were 9.68%, 14.36%, 3.70%, and 6.81%, respectively. The City contributes 65% of the employer cost for police officers, fire employees, and teachers, and the State of New Hampshire contributes the remaining 35% of the employer cost. The City contributes 100% of the employer cost for general employees. In accordance with accounting principles generally accepted in the United States of America (GASB #24), on-behalf fringe benefits contributed by the State of New Hampshire of \$725,639 have been reported as a revenue and expenditure of the General Fund in these financial statements.

Under State law (RSA-100:16), plan member contribution rates are established and may be amended by the New Hampshire State legislature and employer contribution rates are determined by the NHRS Board of Trustees based on an actuarial valuation. The City's contributions to the NHRS for the years ending June 30, 2006, 2005 and 2004 were \$1,953,476, \$1,497,738, and \$1,482,202, respectively, equal to the required contributions for each year.

NOTE 8--GENERAL DEBT OBLIGATIONS

General Long-term Obligations

The changes in the City's long-term debt obligations for the year ended June 30, 2006 are as follows:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

	Balance <u>7/1/2005</u>	<u>Additions</u>	<u>Reductions</u>	Balance <u>6/30/2006</u>	Due Within <u>One Year</u>
Governmental activities:					
Bonds payable	\$ 36,060,361	\$ 17,148,754	\$ (3,668,948)	\$ 49,540,167	\$ 5,143,725
Compensated absences	955,537	434,182	(422,603)	967,116	-
Total governmental activities	<u>\$ 37,015,898</u>	<u>\$ 17,582,936</u>	<u>\$ (4,091,551)</u>	<u>\$ 50,507,283</u>	<u>\$ 5,143,725</u>
Business-type activities:					
Bonds/Notes payable	\$ 28,509,360	\$ 1,824,992	\$ (3,240,016)	\$ 27,094,336	\$ 3,193,557
Total business-type activities	<u>\$ 28,509,360</u>	<u>\$ 1,824,992</u>	<u>\$ (3,240,016)</u>	<u>\$ 27,094,336</u>	<u>\$ 3,193,557</u>

Governmental Activities

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

	Original Issue <u>Amount</u>	Interest <u>Rate</u>	Final Maturity <u>Date</u>	Balance at <u>6/30/06</u>
Capital bond issue #5	\$ 4,605,250	variable	October 2007	\$ 498,675
1991 NHMBB	5,484,100	6.80%	December 2010	1,371,025
1991 NHMBB	13,031,515	6.80%	January 2011	2,865,000
1992 Series D bonds	1,194,500	variable	January 2013	420,000
Refinancing bonds 1994	6,259,500	variable	November 2009	2,059,470
1995 Series bond issue	2,440,000	variable	August 2015	1,200,000
1996 Series bond issue	1,197,000	variable	August 2016	651,000
1997 Series bond issue	1,320,000	variable	August 2017	780,000
1998 Series A	1,779,000	variable	August 2018	1,067,521
2000 Series bond issue	12,084,500	variable	August 2020	5,660,723
2002 Series bond issue	6,383,000	variable	August 2022	5,408,000
2004 Series bond issue	11,169,735	variable	July 2024	10,410,000
2005 Series bond issue - 20 year	3,724,700	variable	January 2026	3,724,700
2005 Series bond issue - 15 year	285,000	variable	January 2021	285,000
2005 Series bond issue - 10 year	2,144,568	variable	January 2016	2,144,568
2005 Series bond issue - Honeywell	9,611,575	variable	January 2016	9,611,575
2005 QZAB	1,382,910	0%	December 2020	1,382,910
Totals	<u>\$ 66,948,100</u>			<u>\$ 49,540,167</u>

Debt service requirements to retire general obligation bonds outstanding at June 30, 2006 are as follows:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Year Ending <u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 5,143,725	\$ 2,290,966	\$ 7,434,691
2008	5,128,197	1,955,157	7,083,354
2009	4,859,317	1,722,461	6,581,778
2010	4,562,838	1,490,906	6,053,744
2011	4,240,641	1,283,730	5,524,371
2012-2016	15,656,286	4,093,469	19,749,755
2017-2021	6,961,163	1,476,582	8,437,745
2022-2026	<u>2,988,000</u>	<u>285,686</u>	<u>3,273,686</u>
Total	<u>\$ 49,540,167</u>	<u>\$ 14,598,957</u>	<u>\$ 64,139,124</u>

Business-type Activities

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

	Issue <u>Amount</u>	Interest <u>Rate</u>	Maturity <u>Date</u>	Balance at <u>6/30/06</u>
Capital bond issue #5	\$ 3,388,450	variable	October 2007	\$ 416,325
1991 NHMBB	615,900	6.80%	January 2011	153,975
1992 Series D bonds	405,500	variable	January 2013	140,000
Refinancing bonds 1994	13,240,500	variable	November 2009	2,340,530
1996 Series bond issue	280,000	variable	August 2016	154,000
1998 Series A	871,000	variable	August 2018	637,480
2000 Series bond issue	1,772,000	variable	August 2020	1,248,777
2002 Series bond issue	2,253,000	variable	August 2022	1,893,000
2002 State Revolving loan fund	19,036,378	variable	August 2020	14,424,422
2004 Series bond issue	2,181,000	variable	July 2024	2,065,000
2005 Series bond issue	261,015	variable	January 2026	261,015
2005 State Revolving loan fund	<u>716,020</u>	variable	January 2015	<u>644,418</u>
Totals	<u>\$ 45,020,763</u>			<u>\$ 24,378,942</u>

Debt service requirements to retire general obligation bonds outstanding, net of principal forgiveness from the State of New Hampshire to be forgiven over a period of 10 years from the start of the individual State Revolving Loan Funds of \$107,403 at June 30, 2006 are as follows:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Year Ending June 30,	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 3,182,817	\$ 999,245	\$ 4,182,062
2008	2,056,486	887,720	2,944,206
2009	1,840,366	796,064	2,636,430
2010	1,566,847	731,910	2,298,757
2011	1,484,043	666,664	2,150,707
2012-2016	6,986,272	2,422,281	9,408,553
2017-2021	6,472,448	961,139	7,433,587
2022-2026	693,000	57,648	750,648
Total	<u>\$ 24,282,279</u>	<u>\$ 7,522,671</u>	<u>\$ 31,804,950</u>

Interest expense for the year ended June 30, 2006 was \$3,185,547 on general obligation debt for the City of Rochester. The State of New Hampshire annually reimburses the City for its share of Sewer related debt service payments. For the year ended June 30, 2006, the reimbursement was \$196,789.

State Revolving Loan

The U.S. Environmental Protection Agency sponsors a low interest rate loan program. The loans are administered by the States and are used by local communities to improve their water systems. In fiscal year 2006, the City borrowed an additional \$1,563,977 through the New Hampshire Water Pollution Control Revolving Fund Program. \$716,020 of the notes payable was converted into general obligation bonds during the year. Total funding to date is \$2,715,394, which is reported as "notes payable" in the Enterprise Funds. Interest is accrued at 1% to be paid upon completion of construction project within the next year.

Authorized and Unissued Debt

The following debt was authorized and unissued as of June 30, 2006:

<u>Purpose</u>	<u>Amount</u>	<u>Total</u>
Governmental Funds:		
2001 Authorized	\$ 235,183	
2002 Authorized	439,000	
2003 Authorized	742,400	
2004 Authorized	1,698,117	
2005 Authorized	7,195,985	
2006 Authorized	4,743,500	
School 2003 Authorized	19,500	
School 2004 Authorized	217,000	
School 2005 Authorized	1,070,000	
School 2006 Authorized	833,000	
Total Governmental		\$ 17,193,685

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

Business-type Funds:	
Sewer 2001 Authorized	\$ 150,000
Sewer 2002 Authorized	209,100
Sewer 2003 Authorized	700,000
Sewer 2004 Authorized	3,330,000
Sewer 2005 Authorized	3,060,500
Sewer 2006 Authorized	3,038,000
Water 2001 Authorized	610,000
Water 2002 Authorized	525,201
Water 2003 Authorized	695,000
Water 2004 Authorized	1,250,000
Water 2005 Authorized	4,244,550
Water 2006 Authorized	4,893,912
Total Business-type	22,706,263
Combining Total	<u>\$ 39,899,948</u>

Available Debt Margin

The City is subject to State statute which limits debt outstanding to a percentage (dependent of purpose) of a valuation calculation made annually by the State. As of June 30, 2006, the City had the following available debt margins:

	Net Debt <u>Outstanding</u>	% of Assessed <u>Valuation</u>	Statutory <u>Limit</u>	Available <u>Debt Limit</u>
School	\$ 23,079,429	7.00%	\$ 166,860,281	\$ 143,780,852
Water	4,438,867	10.00%	238,371,830	233,932,963
All other	27,448,091	3.00%	71,511,549	44,063,458

Per State law, debt incurred for sewer expansion is not included in the limitation calculations.

Overlapping Debt

The City's proportionate share of debt of other governmental units which provide services within the City's boundaries, and which must be borne by the resources of the City, is summarized below (unaudited):

<u>Related Entity</u>	Total <u>Principal</u>	City's <u>Percent</u>	City's <u>Share</u>
Strafford County	<u>\$ 24,942,838</u>	21.541%	<u>\$ 5,372,962</u>

This liability is appropriately not reported in the accompanying financial statements.

NOTE 9--INTERFUND BALANCES

The City has combined the cash resources of its governmental and proprietary fund types. For accounting and reporting purposes, that portion of the pooled cash balance is reposted in the specific finds as an interfund balance. Interfund balances at June 30, 2006 are as follows:

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

	Due from				Totals
	General Fund	Nonmajor Governmental Funds	Sewer Fund	Water Fund	
General Fund		\$ 1,101,122	\$ 2,187,413	\$ 2,067,601	\$ 5,356,136
Capital Projects Fund	\$ 4,293,070				4,293,070
Nonmajor Governmental Funds	3,166,668				3,166,668
Water Fund	763,236				763,236
Sewer Fund	1,921,292			7,619	1,928,911
Arena Fund	59,426				59,426
	<u>\$ 10,203,692</u>	<u>\$ 1,101,122</u>	<u>\$ 2,187,413</u>	<u>\$ 2,075,220</u>	<u>\$ 15,567,447</u>

NOTE 10--INTERFUND TRANSFERS

During the year, several interfund transactions occurred between funds. The various operating transfers were made in accordance with budgetary authorizations. Interfund transfers for the year ended June 30, 2006 are as follows:

	Transfer from			Totals
	General Fund	Capital Projects Fund	Nonmajor Governmental Funds	
General Fund		\$ 365,057		\$ 365,057
Capital Projects Fund	\$ 227,500		158,500	386,000
Nonmajor Governmental Funds	357,582	245,358		602,940
	<u>\$ 585,082</u>	<u>\$ 610,415</u>	<u>\$ 158,500</u>	<u>\$ 1,353,997</u>

NOTE 11--RESTRICTED NET ASSETS

Net assets are restricted for specific purposes as follows:

	Governmental Activities
Endowments	\$ 38,331
Special Revenue Funds	3,125,051
Capital Projects	3,533,145
	<u>\$ 6,696,527</u>

NOTE 12--PERMANENT FUNDS

Cemetery care funds are accounted for as permanent funds. The principal amounts of all cemetery finds are restricted in that only income earned may be expended. Principal and income balances at June 30, 2006 are as follows:

	Principal	Income	Total
Cemetery Funds	<u>\$ 38,331</u>	<u>\$ 12,884</u>	<u>\$ 51,215</u>

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

NOTE 13--RESERVED FOR SPECIAL PURPOSES

The balance reserved for special purposes in the General fund at June 30, 2006 is as follows:

Computer Purchases	\$ <u>20,000</u>
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NOTE 14--RESTATEMENT OF EQUITY

Correction of an Error

Government-Wide Financial Statements

Net assets of the General Fund have been restated as of July 1, 2005 because of an error in the amount of compensated absences recorded and an overstatement of accrued payroll. Net assets of the governmental activities as of July 1, 2005 have been restated as follows:

	<u>Governmental</u> <u>Activities</u>
Balance, July 1 - as previously reported	\$ 50,300,850
Amount of restatement due to:	
Overstatement of compensated absences	174,426
Overstatement of accrued payroll	<u>85,697</u>
Balance, July 1 - as restated	<u>\$ 50,560,973</u>

Fund Financial Statements

During the year ended June 30, 2006, it was determined that the accrued payroll in the General Fund was overstated. Fund balance of the General Fund as of July 1, 2005 has been restated as follows:

	<u>General</u> <u>Fund</u>
Fund Balance, July 1, 2005 (as previously reported)	\$ 5,473,428
Amount of restatement due to:	
Overstatement of accrued payroll	<u>85,697</u>
Fund Balance, July 1, 2005 - as restated	<u>\$ 5,559,125</u>

NOTE 15--CONTINGENT LIABILITIES

The City is involved in a lawsuit with Waste Management of New Hampshire, Inc., the owner of the Turnkey Landfill facility in Rochester, New Hampshire. Waste Management of New Hampshire, Inc. alleges that it has invested approximately \$45,000,000 in pollution control facilities at its Turnkey Landfill site therefore qualifying for a real estate tax exemption for the cost of such facilities for a period of 25 years under the terms of RSA 72:12-a. The assessed value of the Turnkey Landfill is currently approximately \$39,000,000. Consequently, if the exemption request was to be granted, it is conceivable that the assessed value of the City of Rochester could be reduced by approximately \$39,000,000.

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
For the Year Ended June 30, 2006

The City is also involved in a lawsuit with Verizon (formerly Bell Atlantic) for the abatement of its 1996 through 2000 property taxes. The Taxpayer alleges that the taxation of the land that houses the poles and wires is illegal. The New Hampshire Supreme Court ruled in 1999 that the land located in public rights of way occupied by utilities is taxable. This ruling has been appealed by the Taxpayer. The City has recorded a reserve for the amount of total taxes unpaid of \$1,839,205.

The City participates in a number of federally assisted grant programs. These programs are subject to financial and compliance audits by the grantors or their representatives. The amounts, if any, of expenditures which may be disallowed by the granting agency cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

SCHEDULE 1

CITY OF ROCHESTER, NEW HAMPSHIRE

Statement of Revenues, Expenditures and Changes in Fund Balances

Budget and Actual (Budgetary Basis) - General Fund

For the Year Ended June 30, 2006

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Favorable (Unfavorable)
	Original	Final		
Revenues:				
Taxes	\$ 37,916,629	\$ 38,164,561	\$ 38,421,656	\$ 257,095
Licenses and permits	4,618,445	4,618,445	4,793,221	174,776
Intergovernmental	21,087,823	21,087,823	21,469,101	381,278
Charges for services	670,206	670,206	680,489	10,283
Interest income	375,000	375,000	870,238	495,238
Miscellaneous	2,581,326	2,581,326	2,717,430	136,104
Total Revenues	<u>67,249,429</u>	<u>67,497,361</u>	<u>68,952,135</u>	<u>1,454,774</u>
Expenditures:				
Current:				
General government	3,575,298	3,474,041	3,176,383	297,658
Public safety	9,004,839	8,974,096	8,740,375	233,721
Highways and streets	2,284,037	2,349,837	2,220,418	129,419
Health and welfare	642,296	774,296	788,185	(13,889)
Culture and recreation	1,495,522	1,495,522	1,463,474	32,048
Community development	96,507	96,507	97,193	(686)
Education	41,177,422	41,177,422	40,403,810	773,612
Debt service:				
Principal retirement	3,696,993	3,696,993	3,668,948	28,045
Interest and fiscal charges	1,742,558	1,742,558	1,742,558	-
Intergovernmental	4,379,097	4,379,097	4,379,097	-
Total Expenditures	<u>68,094,569</u>	<u>68,160,369</u>	<u>66,680,441</u>	<u>1,479,928</u>
Excess revenues over (under) expenditures	<u>(845,140)</u>	<u>(663,008)</u>	<u>2,271,694</u>	<u>2,934,702</u>
Other financing uses:				
Operating transfers in	365,057	365,057	365,057	-
Operating transfers out	<u>(207,500)</u>	<u>(455,432)</u>	<u>(585,082)</u>	<u>(129,650)</u>
Total other financing uses	<u>157,557</u>	<u>(90,375)</u>	<u>(220,025)</u>	<u>(129,650)</u>
Excess revenues over (under) expenditures and other uses	<u>(687,583)</u>	<u>(753,383)</u>	<u>2,051,669</u>	<u>2,805,052</u>
Fund balances at beginning of year				
- Budgetary Basis	<u>5,867,505</u>	<u>5,867,505</u>	<u>5,867,505</u>	<u>-</u>
Fund balances at end of year				
- Budgetary Basis	<u>\$ 5,179,922</u>	<u>\$ 5,114,122</u>	<u>\$ 7,919,174</u>	<u>\$ 2,805,052</u>

See accompanying notes to the required supplementary information

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
June 30, 2006

NOTE 1—BUDGET TO ACTUAL RECONCILIATION

General Fund

Amounts recorded as budgetary amounts in the Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual (Budgetary Basis) – General Fund (Schedule 1) are reported on the basis budgeted by the City. Those amounts differ from those reported in conformity with accounting principles generally accepted in the United States of America in the Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds (Exhibit D). Property tax budgetary revenues are recognized when levied rather than when susceptible to accrual. General Fund budgetary expenditures were adjusted for on-behalf payments for fringe benefits as follows:

	Revenues <u>and Transfers</u>	Expenditures <u>and Transfers</u>
Exhibit D	\$ 69,761,383	\$ 67,991,162
Difference in property taxes meeting susceptible to accrual criteria	281,448	
On-behalf fringe benefits	<u>(725,639)</u>	<u>(725,639)</u>
Schedule 1	<u>\$ 69,317,192</u>	<u>\$ 67,265,523</u>

SCHEDULE I
CITY OF ROCHESTER, NEW HAMPSHIRE
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2006

Federal Granting Agency/Recipient State Agency/Grant Program/State Grant Number	Federal Catalogue Number	Expenditures
DEPARTMENT OF AGRICULTURE		
Pass Through Payments from New Hampshire Department of Education		
National School Lunch Program	10.555	\$ 493,117
School Breakfast Program	10.553	84,501
Food Distribution	10.550	65,142
Food Donation	10.559	4,890
Summer Food Service Program for Children	10.556	46,829
		<u>694,479</u>
Wildlife Habitat Incentive Program	10.914	<u>14,630</u>
Total Department of Agriculture		<u>709,109</u>
DEPARTMENT OF EDUCATION		
Pass Through Payments from New Hampshire Department of Education		
Adult Education - State Grant Program #67315	84.002	<u>3,429</u>
Title I Grants to Local Educational Agencies #50012	84.010	118,159
#50140		9,827
#50226		16,197
#54028		2,322
#60113		1,015,654
#60189		35
#60210		64,905
#60701		34,823
#64036		3,361
		<u>1,265,283</u>
Special Education - Grants to States	84.027	
	84.173	
#52585		15,812
#62510		956,078
#52770		971
#62708		1,344
#62717		44,040
		<u>1,018,245</u>
Special Education - Education for Homeless Children and Youth #50701	84.196A	<u>5,032</u>
Vocational Education - Basic Grants to States #55041	84.048A	15,539
#65036		145,607
		<u>161,146</u>
Safe and Drug-Free Schools - State Grants #Q184E040084	84.184E	<u>8,674</u>
Safe and Drug-Free Schools and Communities #66596	84.186	<u>37,206</u>
Safe and Drug-Free Schools - State Grants #55075	84.243A	<u>55</u>

See notes to schedule of expenditures of federal awards

SCHEDULE I
CITY OF ROCHESTER, NEW HAMPSHIRE
Schedule of Expenditures of Federal Awards (Continued)
For the Year Ended June 30, 2006

Federal Granting Agency/Recipient State Agency/Grant Program/State <u>Grant Number</u>	Federal Catalogue <u>Number</u>	<u>Expenditures</u>
Innovated Education Program Strategies	84.298A	
#56127		8,271
#66127		20,270
		<u>28,541</u>
Education Technology State Grants	84.318X	
#54547		57,059
		<u>57,059</u>
Reading First State Grants	84.357A	
#50758		129,593
#60758		180,658
#60759		2,764
#60760		17,178
		<u>330,193</u>
Improving Teacher Quality Grants	84.367A	
#54913		59,468
#64913		223,817
		<u>283,285</u>
Total Department of Education		<u>3,198,148</u>
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT		
Received directly from U.S. Treasury Department		
Community Development Block Grants - Entitlement Grants		
#B-03-MC33-0004	14.218	118,016
#B-04-MC33-0004		134,131
		<u>252,147</u>
Pass Through Payments from the Rochester Housing Authority		
Public Housing Capital Fund	14.872	
#50100		63,392
		<u>63,392</u>
Total Department of Housing and Urban Development		<u>315,539</u>
DEPARTMENT OF JUSTICE		
Pass Through Payments from the New Hampshire Office of the Governor and Attorney General		
Local Law Enforcement Block Grants Program	16.592	
#2003-LB-BX-1569		35
#2003-LB-BX-1475		1,567
		<u>1,602</u>
		<u>1,602</u>
Total Department of Justice		<u>1,602</u>
DEPARTMENT OF HOMELAND SECURITY		
Pass Through Payments from New Hampshire Office of Emergency Management		
Homeland Security Grant Program	97.067	12,136
		<u>12,136</u>
Total Department of Homeland Security		<u>12,136</u>
Total Expenditures of Federal Awards		<u>\$ 4,236,534</u>

See notes to schedule of expenditures of federal awards

CITY OF ROCHESTER, NEW HAMPSHIRE
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
June 30, 2006

NOTE 1--GENERAL

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the City of Rochester, New Hampshire. The City of Rochester's reporting entity is defined in Note 1 to the City's basic financial statements.

NOTE 2--BASIS OF ACCOUNTING

The accompanying Schedule of Expenditures of Federal Awards is presented using the modified accrual basis of accounting, which is described in Note 1 to the City's basic financial statements.

NOTE 3--NON-CASH TRANSACTIONS

The Food Distribution Program (CFDA #10.550) is a non-cash program. Dollar values reported on the Schedule of Expenditures of Federal Awards (\$65,142) represent the value of commodities used by the City from this program.

NOTE 4--RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

The recognition of expenditures of federal awards has been reported in the City's basic financial statements as intergovernmental revenues in the Nonmajor Special Revenue Funds as follows:

Major Funds:	
Capital Projects Fund	\$ 14,630
Nonmajor Funds:	
CDBG Fund	252,147
Federal Projects Fund	3,198,148
Food Service Fund	694,479
Homeland Security Grants Fund	12,136
Police Grants Fund	64,994
	<u>\$ 4,236,534</u>

Vachon, Clukay & Co., PC

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS***

To the Honorable Mayor, City Council and Manager
City of Rochester, New Hampshire

We have audited the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Rochester, New Hampshire, as of and for the year ended June 30, 2006, and have issued our report thereon dated October 25, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Rochester, New Hampshire's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level of risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Rochester, New Hampshire's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Honorable Mayor and City Council, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Vachon, Cleary & Co., PC

October 25, 2006

Vachon, Clukay & Co., PC

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Honorable Mayor, City Council and Manager
City of Rochester, New Hampshire

Compliance

We have audited the compliance of the City of Rochester, New Hampshire with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2006. The City of Rochester, New Hampshire's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City of Rochester, New Hampshire's management. Our responsibility is to express an opinion on the City of Rochester, New Hampshire's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Rochester, New Hampshire's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Rochester, New Hampshire's compliance with those requirements.

In our opinion, the City of Rochester, New Hampshire complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2006.

Internal Control Over Compliance

The management of the City of Rochester, New Hampshire is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City

of Rochester, New Hampshire's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management, the Honorable Mayor and City Council, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Vachon, Clark & Co. PC

October 25, 2006

**City of Rochester, New Hampshire
Schedule of Findings and Questioned Costs
Year Ended June 30, 2006**

Section I--Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: unqualified

Internal control over financial reporting:

 Material weakness(es) identified? _____yes X no

 Reportable condition(s) identified
 not considered to be material weaknesses? _____yes X none reported

Noncompliance material to financial statements noted? _____yes X no

Federal Awards

Internal Control over major programs:

 Material weakness(es) identified? _____yes X no

 Reportable condition(s) identified
 not considered to be material weaknesses? _____yes X none reported

Type of auditor's report issued on compliance
 for major programs: unqualified

Any audit findings disclosed that are required
 to be reported in accordance with
 Circular A-133, Section .510(a)? _____yes X no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
84.010	Title I Grants to Local Educational Agencies
84.027 & 84.173	Special Education – Grants to States

Dollar threshold used to distinguish
 between Type A and Type B program: \$ 300,000

Auditee qualified as low-risk auditee? _____X yes _____ no

Section II--Financial Statement Findings

There were no findings relating to the financial statements required to be reported by GAGAS.

Section III--Federal Award Findings and Questioned Costs

There were no findings and questioned costs as defined under OMB Circular A-133 .510(a).