

Washington State Auditor's Office
Financial Statements and Federal Single Audit Report

City of Chehalis
Lewis County

Audit Period
January 1, 2006 through December 31, 2006

Report No. 73821

Issue Date
December 31, 2007



WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

December 31, 2007

Mayor and City Council
City of Chehalis
Chehalis, Washington

Report on Financial Statements and Federal Single Audit

Please find attached our report on the City of Chehalis' financial statements and compliance with federal laws and regulations.

We are issuing this report in order to provide information on the City's financial condition.

In addition to this work, we look at other areas of our audit client's operations for compliance with state laws and regulations. The results of that audit will be included in a separately issued accountability report.

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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Lewis County
January 1, 2006 through December 31, 2006**

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Federal Summary

**City of Chehalis
Lewis County
January 1, 2006 through December 31, 2006**

The results of our audit of the City of Chehalis are summarized below in accordance with U.S. Office of Management and Budget Circular A-133.

FINANCIAL STATEMENTS

An unqualified opinion was issued on the financial statements.

Internal Control Over Financial Reporting:

- **Significant Deficiencies:** We reported no deficiencies in the design or operation of internal control over financial reporting that we consider to be significant deficiencies.
- **Material Weaknesses:** We identified no significant deficiencies that we consider to be material weaknesses.

We noted no instances of noncompliance that were material to the financial statements of the City.

FEDERAL AWARDS

Internal Control Over Major Programs:

- **Significant Deficiencies:** We reported no deficiencies in the design or operation of internal control over major federal programs that we consider to be significant deficiencies.
- **Material Weaknesses:** We identified no significant deficiencies that we consider to be material weaknesses.

We issued an unqualified opinion on the City's compliance with requirements applicable to its major federal program.

We reported no findings that are required to be disclosed under OMB Circular A-133.

Identification of Major Programs:

The following was a major program during the period under audit:

<u>CFDA No.</u>	<u>Program Title</u>
66.458	Capitalization Grants for Clean Water State Revolving Funds

The dollar threshold used to distinguish between Type A and Type B programs, as prescribed by OMB Circular A-133, was \$380,734.

The City did not qualify as a low-risk auditee under OMB Circular A-133.

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

City of Chehalis
Lewis County
January 1, 2006 through December 31, 2006

Mayor and City Council
City of Chehalis
Chehalis, Washington

We have audited the financial statements of the City of Chehalis, Lewis County, Washington, as of and for the year ended December 31, 2006, and have issued our report thereon dated December 14, 2007.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the 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's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of the City's compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended for the information and use of management, the Mayor and City Council, federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag", is positioned above the printed name and title.

BRIAN SONNTAG, CGFM
STATE AUDITOR

December 14, 2007

Independent Auditor's Report on Compliance with Requirements Applicable to its Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133

**City of Chehalis
Lewis County
January 1, 2006 through December 31, 2006**

Mayor and City Council
City of Chehalis
Chehalis, Washington

COMPLIANCE

We have audited the compliance of the City of Chehalis, Lewis County, Washington, 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 its major federal program for the year ended December 31, 2006. The City's major federal program is identified in the Federal Summary. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the City's management. Our responsibility is to express an opinion on the City'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 the 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'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's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2006.

INTERNAL CONTROL OVER COMPLIANCE

The management of the City 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's internal control over compliance with the 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 internal control over compliance, but not for the purpose of expressing an opinion on the

effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is a more than remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in a more than remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended for the information of management, the Mayor and City Council, federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

BRIAN SONNTAG, CGFM
STATE AUDITOR

December 14, 2007

Independent Auditor's Report on Financial Statements

City of Chehalis Lewis County January 1, 2006 through December 31, 2006

Mayor and City Council
City of Chehalis
Chehalis, Washington

We have audited the accompanying financial statements of the City of Chehalis, Lewis County, Washington, as of and for the year ended December 31, 2006, as listed on page 8. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As described in Note 1 to the financial statements, the City prepares its financial statements using accounting practices prescribed by Washington State statutes and the *Budgeting, Accounting and Reporting System* (BARS) manual prescribed by the State Auditor, which demonstrates compliance with the regulatory basis of accounting which differs from accounting principles generally accepted in the United States of America. The differences between the regulatory basis of accounting and the accounting principles generally accepted in the United States of America are also described in Note 1.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Chehalis, as of December 31, 2006, and the changes in financial position and, where applicable, cash flows, thereof, and the respective budgetary comparison for the General and Public Facilities Reserve funds, for the year then ended on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report 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.

Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. 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*. This schedule is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit

of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

This report is intended for the information and use of the governing body and management of the City. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag", with a stylized, cursive script.

BRIAN SONNTAG, CGFM
STATE AUDITOR

December 14, 2007

Financial Section

**City of Chehalis
Lewis County
January 1, 2006 through December 31, 2006**

FINANCIAL STATEMENTS

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Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds – 2006
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Statement of Cash Flows – Proprietary Funds – 2006
Statement of Fiduciary Net Assets – Fiduciary Funds – 2006
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Notes to Financial Statements – 2006

SUPPLEMENTAL INFORMATION

Schedule of Expenditures of Federal Awards – 2006
Notes to the Schedule of Expenditures of Federal Awards – 2006

CITY OF CHEHALIS
Balance Sheet
Governmental Funds
December 31, 2006

	<u>MAJOR FUNDS</u>		<u>OTHER</u>	<u>TOTAL</u>
	<u>GENERAL</u>	<u>PUBLIC</u>	<u>NON-MAJOR</u>	<u>FUNDS</u>
	<u>FUND</u>	<u>FACILITIES</u>	<u>FUNDS</u>	
ASSETS				
Current Assets				
Cash and cash equivalents	\$ 1,076,935	\$ 3,725	\$ 1,236,249	\$ 2,316,909
Investments -ST	169,521		1,213,129	1,382,650
Receivable				
Taxes	38,925			38,925
Accounts	2,049			2,049
Other	135,906			135,906
Notes			10,071	10,071
Long-Term assets				
Investments -LT	113,976			113,976
Notes/contracts receivable			411,746	411,746
TOTAL ASSETS	<u>\$ 1,537,312</u>	<u>\$ 3,725</u>	<u>\$ 2,871,195</u>	<u>\$ 4,412,232</u>
LIABILITIES and FUND BALANCE				
Current Liabilities:				
Accounts payable	\$ 88,500	\$ 3,455	\$ 5,163	\$ 97,118
Due to other governments	(15)			(15)
Compensated absences payable	147,747			147,747
Other Current liabilities	1,875			1,875
Deferred revenue	174,831		421,818	596,649
TOTAL LIABILITIES	<u>412,938</u>	<u>3,455</u>	<u>426,981</u>	<u>843,374</u>
Fund Balance				
Reserved for:				
Equipment			494,559	494,559
Other purposes		270	719,948	720,218
Unreserved, Reported in:			-	-
Major funds	1,124,374		1,229,706	2,354,080
TOTAL FUND BALANCE	<u>1,124,374</u>	<u>270</u>	<u>2,444,213</u>	<u>3,568,857</u>
TOTAL LIABILITIES AND FUND BALANCE	<u>\$ 1,537,312</u>	<u>\$ 3,725</u>	<u>\$ 2,871,194</u>	<u>\$ 4,412,231</u>

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

CITY OF CHEHALIS
Statement of Revenues, Expenses, and Changes in Fund Balance
Governmental Funds
For the year ended December 31, 2006

	MAJOR FUNDS		OTHER NON-MAJOR FUNDS	TOTAL FUNDS
	GENERAL FUND	PUBLIC FACILITIES		
Revenues:				
Taxes	\$ 6,052,538	\$ 101,269	\$ 523,590	\$ 6,677,397
Licenses and permits	182,127			182,127
Intergovernmental	279,816		136,684	416,500
Charges for services	784,106		76,786	860,892
Fines and forfeitures	117,331			117,331
Rents	87,438		105,783	193,221
Other revenue	146,665	103,254	3,794	253,713
Total Revenues	<u>7,650,021</u>	<u>204,523</u>	<u>846,637</u>	<u>8,701,181</u>
Expenditures:				
General government	1,947,841	19,177	84,155	2,051,173
Security of persons and property	3,757,739	24,137	1,060	3,782,936
Physical environment	46,810			46,810
Transportation	707,135		38,454	745,589
Economic environment	191,027		217,656	408,683
Mental & physical health	1,507			1,507
Culture & recreation	1,100,737			1,100,737
Interest & debt service	70,758	79,227		149,985
Capital outlay	36,451	725,910	108,204	870,565
Total expenditures	<u>7,860,005</u>	<u>848,451</u>	<u>449,529</u>	<u>9,157,985</u>
Excess (deficiency) of revenues over expenditures	(209,984)	(643,928)	397,108	(456,804)
Other financing sources (uses)				
Operating transfers in	49,213	503,750	1,207,727	1,760,690
Operating transfers out	(83,500)	(781,920)	(621,750)	(1,487,170)
Total other financing sources (uses)	<u>(34,287)</u>	<u>(278,170)</u>	<u>585,977</u>	<u>273,520</u>
Net change in fund balances	(244,271)	(922,098)	983,085	(183,284)
Fund Balances - Beginning	1,368,644	922,368	1,461,129	3,752,141
Fund Balances - Ending	<u>\$ 1,124,373</u>	<u>\$ 270</u>	<u>\$ 2,444,214</u>	<u>\$ 3,568,857</u>

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

CITY OF CHEHALIS
Statement of Revenues, Expenditures, and Changes in Fund Balance
Major Fund - General Fund
Budget and Actual
For the Year Ended December 31, 2006

	BUDGETED AMOUNTS		ACTUAL AMOUNTS	VARIANCE FAVORABLE (UNFAVORABLE)
	ORIGINAL	FINAL		
Revenues:				
Taxes	\$ 6,009,990	\$ 6,009,990	\$ 6,052,538	\$ 42,548
Licenses and permits	89,560	89,560	182,127	92,567
Intergovernmental	322,149	322,149	279,816	(42,333)
Charges for services	767,140	767,140	784,106	16,966
Fines and forfeitures	109,700	109,700	117,331	7,631
Rents	43,400	43,400	87,438	44,038
Other revenue	52,200	52,200	146,665	94,465
Total Revenues	<u>7,394,139</u>	<u>7,394,139</u>	<u>7,650,021</u>	<u>255,882</u>
Expenditures:				
General government	1,713,618	1,817,618	1,947,841	(130,223)
Security of persons and property	3,796,066	3,841,066	3,757,739	83,327
Physical environment	72,200	72,200	46,810	25,390
Transportation	747,613	747,613	707,135	40,478
Economic environment	182,875	182,875	191,027	(8,152)
Mental & physical health	1,600	1,600	1,507	93
Culture & recreation	1,058,286	1,088,286	1,100,737	(12,451)
Interest & debt service	70,758	70,758	70,758	0
Capital outlay	20,400	20,400	36,451	(16,051)
Total expenditures	<u>7,663,416</u>	<u>7,842,416</u>	<u>7,860,005</u>	<u>(17,589)</u>
Excess (deficiency) of revenues over expenditures	<u>(269,277)</u>	<u>(448,277)</u>	<u>(209,984)</u>	<u>238,293</u>
Other financing sources (uses)				
Operating transfers in	80,728	80,728	49,213	(31,515)
Operating transfers out	(83,500)	(83,500)	(83,500)	0
Total other financing sources (uses)	<u>(2,772)</u>	<u>(2,772)</u>	<u>(34,287)</u>	<u>(31,515)</u>
Net Change in Fund Balance	<u>(272,049)</u>	<u>(451,049)</u>	<u>(244,271)</u>	<u>206,778</u>
Fund Balance - Beginning	<u>1,368,644</u>	<u>1,368,644</u>	<u>1,368,644</u>	<u>-</u>
Fund Balance - Ending	<u>\$ 1,096,595</u>	<u>\$ 917,595</u>	<u>\$ 1,124,373</u>	<u>\$ 206,778</u>

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

CITY OF CHEHALIS
Statement of Revenues, Expenditures, and Changes in Fund Balance
Major Fund - Public Facilities Reserve
Budget and Actual
For the Year Ended December 31, 2006

	BUDGETED AMOUNTS		ACTUAL	VARIANCE
	ORIGINAL	FINAL	AMOUNTS	FAVORABLE (UNFAVORABLE)
Revenues:				
Taxes	\$ 100,000	\$ 100,000	\$ 101,269	\$ 1,269
Licenses and permits	-	-	-	-
Intergovernmental	-	-	-	-
Charges for services	-	-	-	-
Fines and forfeitures	-	-	-	-
Rents	-	-	-	-
Other revenue	10,000	10,000	103,254	93,254
Total Revenues	110,000	110,000	204,523	94,523
Expenditures:				
General government	-	-	\$ 19,177	(19,177)
Security of persons and property	36,000	36,000	24,137	11,863
Physical environment	-	-	-	-
Transportation	-	-	-	-
Economic environment	-	-	-	-
Mental & physical health	-	-	-	-
Culture & recreation	-	-	-	-
Interest & debt service	-	-	79,227	(79,227)
Capital outlay	313,000	728,000	725,910	2,090
Total expenditures	349,000	764,000	848,451	(84,451)
Excess (deficiency) of revenues over expenditures	(239,000)	(654,000)	(643,928)	10,072
Other financing sources (uses)				
Operating transfers in	250,000	650,000	503,750	(146,250)
Operating transfers out	(758,234)	(758,234)	(781,920)	(23,686)
Total other financing sources (uses)	(508,234)	(108,234)	(278,170)	(169,936.00)
Net Change in Fund Balance	(747,234)	(762,234)	(922,098)	(159,864)
Fund Balance - Beginning	922,368	922,368	922,368	-
Fund Balance - Ending	\$ 175,134	\$ 160,134	\$ 270	\$ (159,864)

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

CITY OF CHEHALIS
STATEMENT OF NET ASSETS
Proprietary Funds
December 31, 2006

	Business-Type Activities Enterprise Funds				
	Garbage	Wastewater	Water	Storm Drainage	Totals
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	\$ 16,628	1,494,587	798,357	359,243	2,668,815
Accounts receivable (net):					
Customer accounts receivable (net)	31,894	345,590	423,259	13,054	813,797
Interest receivable			1,209		1,209
Inventory		15,220	85,527		100,747
Short-term investments			1,741,361		1,741,361
Total current assets	<u>48,522</u>	<u>1,855,397</u>	<u>3,049,713</u>	<u>372,297</u>	<u>5,325,929</u>
Restricted assets:					
Customer deposits - cash & equivalents			121,370		121,370
Customer deposits - investments			175,000		175,000
Revenue bonds - cash & equivalents			132,579		132,579
Total restricted assets	<u>-</u>	<u>-</u>	<u>428,949</u>	<u>-</u>	<u>428,949</u>
NONCURRENT ASSETS:					
Land		4,082,233	150,168	267	4,232,668
Depreciable capital assets	6,312	21,127,565	5,750,616	110,216	26,994,709
Construction in progress		33,080,075	1,297,141		34,377,216
Total capital assets (net)	<u>6,312</u>	<u>58,289,873</u>	<u>7,197,925</u>	<u>110,483</u>	<u>65,604,593</u>
Long-term investments			825,000	-	825,000
Total noncurrent assets	<u>6,312</u>	<u>58,289,873</u>	<u>8,022,925</u>	<u>110,483</u>	<u>66,429,593</u>
TOTAL ASSETS	\$ 54,834	\$ 60,145,270	\$ 11,501,587	\$ 482,780	\$ 72,184,471
LIABILITIES					
CURRENT LIABILITIES:					
Accounts payable	\$ 25,514	826,956	57,469	3,783	913,722
Revenues collected in advance			28,232		28,232
Due to other governments	-	218,737	49,915		268,652
Notes payable - current portion		1,071,881			1,071,881
Accrued employee benefits	-	19,924	39,615	3,335	62,874
Interest payable		28,889	10,375		39,264
Other current liabilities		7	7		14
Total current liabilities	<u>25,514</u>	<u>2,166,394</u>	<u>185,613</u>	<u>7,118</u>	<u>2,384,639</u>
Current liabilities payable from restricted assets:					
Bonds payable			14,000		14,000
Customer deposits			297,942		297,942
Total current liabilities payable from restr. assets	<u>-</u>	<u>-</u>	<u>311,942</u>	<u>-</u>	<u>311,942</u>
NONCURRENT LIABILITIES:					
Interest payable					-
Bonds payable			227,000		227,000
Due to other governments		29,807,170	650,008		30,457,178
Notes payable		497,266	-		497,266
Employee leave benefits	-	24,446	38,427	9,874	72,747
Total noncurrent liabilities	<u>-</u>	<u>30,328,882</u>	<u>915,435</u>	<u>9,874</u>	<u>31,254,191</u>
TOTAL LIABILITIES	\$ 25,514	\$ 32,495,276	\$ 1,412,990	\$ 16,992	\$ 33,950,772
NET ASSETS					
Invested in capital assets, net of related debt	\$ 6,312	26,694,819	6,257,002	110,483	33,068,616
Unrestricted	23,008	955,175	3,831,595	355,305	5,165,083
TOTAL NET ASSETS	\$ 29,320	\$ 27,649,994	\$ 10,088,597	\$ 465,788	\$ 38,233,699

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

CITY OF CHEHALIS
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended December 31, 2006

	Enterprise Funds				
	Garbage	Wastewater	Water	Storm	Totals
Operating revenue:					
Intergovernmental		160,578	7,815		168,393
Charges for services	327,264	2,805,549	2,085,627	369,302	5,587,742
Miscellaneous revenue		10,338	125	553	11,016
Cost contributions		89,809	107,071	8,054	204,934
Total operating revenue	327,264	3,066,274	2,200,638	377,909	5,972,085
Operating expenses:					
Operations and maintenance	341,390	2,234,168	1,265,900	248,449	4,089,907
Administration/overhead		213,830	122,727		336,557
Taxes	4,815	310,178	232,445	8,282	555,720
Depreciation		736,940	263,551	6,186	1,006,677
Total operating expenses	346,205	3,495,116	1,884,623	262,917	5,988,861
Operating income (loss)	(18,941)	(428,842)	316,015	114,992	(16,776)
Nonoperating revenues (expenses):					
Interest revenue	22	137,680	77,922	26,799	242,423
Interest expense/fiscal charges		(200,901)	(66,030)		(266,931)
Gain (loss) on disposal of fixed assets		2,102,477			2,102,477
Total nonoperating revenues (expenses)	22	2,039,256	11,892	26,799	2,077,969
Income (loss) before contributions and transfers	(18,919)	1,610,414	327,907	141,791	2,061,193
Capital contributions		2,060,159			2,060,159
Transfers In		283,410			283,410
Transfers out	(1,055)	(456,199)	(33,704)		(490,958)
Change in net assets	(19,974)	3,497,784	294,203	141,791	3,913,804
Total net assets - beginning, as previously reported	49,294	23,999,078	9,794,394	323,997	34,166,763
Prior period adjustments		153,132			153,132
Total net assets - beginning, as adjusted	49,294	24,152,210	9,794,394	323,997	34,319,895
Total net assets - ending	29,320	27,649,994	10,088,597	465,788	38,233,699

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

CITY OF CHEHALIS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
For the Year Ended December 31, 2006

	Business-type Activities Enterprise Funds				
	Garbage	Wastewater	Water	Storm	Totals
CASH FLOWS FROM OPERATING ACTIVITIES:					
Cash received from customers	\$ 325,560	\$ 3,040,113	\$ 2,168,118	\$ 376,717	\$ 5,910,508
Cash payments to suppliers	(329,127)	(2,302,353)	(983,843)	(116,940)	(3,732,263)
Cash payments to employees	-	(998,464)	(472,214)	(105,556)	(1,576,234)
Internal activity - payments to other funds	(17,500)	(193,000)	(114,000)	(38,500)	(363,000)
Net cash provided (used) by operating activities	(21,067)	(453,704)	598,061	115,721	239,011
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:					
Cash transfers from other funds	-	-	-	-	-
Cash transfers to other funds	(1,055)	-	(33,704)	-	(34,759)
Net cash used by noncapital financing activities	(1,055)	-	(33,704)	-	(34,759)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:					
Acquisition and construction of capital assets	\$ (6,312)	\$ (18,798,214)	\$ (212,102)	\$ (6,313)	\$ (19,022,941)
Proceeds from sale of capital assets	-	2,468,274	-	-	2,468,274
Capital contributions	-	2,060,159	-	-	2,060,159
Proceeds from issuance of long-term debt	-	18,517,745	37,402	-	18,555,147
Principal paid on long-term debt	-	(3,554,797)	(59,329)	-	(3,614,126)
Cash paid for interest on debt	-	(176,470)	(30,248)	-	(206,718)
Net cash provided (used) by capital and related financing activities	(6,312)	516,697	(264,277)	(6,313)	239,795
CASH FLOWS FROM INVESTING ACTIVITIES:					
Cash receipts from interest earnings	\$ 22	\$ 137,680	\$ 76,871	\$ 26,799	241,372
Cash received from investment sales	-	2,609,724	1,110,000	127,000	3,846,724
Cash paid for investment acquisition	-	(1,350,000)	(746,000)	(100,000)	(2,196,000)
Net cash provided by investing activities	22	1,397,404	440,871	53,799	1,892,096
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(28,412)	1,460,397	740,951	163,207	2,336,143
CASH AND CASH EQUIVALENTS - BEGINNING	45,040	34,190	311,355	196,036	586,621
CASH AND CASH EQUIVALENTS - ENDING	<u>\$ 16,628</u>	<u>\$ 1,494,587</u>	<u>\$ 1,052,306</u>	<u>\$ 359,243</u>	<u>\$ 2,922,764</u>
Operating fund cash and cash equivalents	\$ 16,628	\$ 1,494,587	\$ 798,357	\$ 359,243	2,668,815
Restricted funds cash and cash equivalents	-	-	253,949	-	253,949
CASH AND CASH EQUIVALENTS - ENDING	<u>\$ 16,628</u>	<u>\$ 1,494,587</u>	<u>\$ 1,052,306</u>	<u>\$ 359,243</u>	<u>\$ 2,922,764</u>

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

CITY OF CHEHALIS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
For the Year Ended December 31, 2006

	Business-type Activities Enterprise Funds				Totals
	Garbage	Wastewater	Water	Storm	
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:					
Net operating income (loss)	\$ (18,941)	\$ (428,842)	\$ 316,015	\$ 114,992	\$ (16,776)
Adjustments to reconcile net operating income to net cash provided (used) by operations:					
Depreciation	-	736,940	263,551	6,186	1,006,677
(Increase) decrease in accounts receivable	(1,704)	(26,161)	(50,270)	(1,192)	(79,327)
(Increase) decrease in inventory	-	1,529	12,917	-	14,446
Increase (decrease) in accounts payable	423	(716,546)	28,056	781	(687,286)
Increase (decrease) in accrued employee benefits	(845)	(20,624)	10,042	(5,046)	(16,473)
Increase (decrease) in customer deposits		-	10,779	-	10,779
Increase (decrease) in revenues collected in advance		-	6,971	-	6,971
Total adjustments	(2,126)	(24,862)	282,046	729	255,787
Net cash provided (used) by operating activities	<u>\$ (21,067)</u>	<u>\$ (453,704)</u>	<u>\$ 598,061</u>	<u>\$ 115,721</u>	<u>\$ 239,011</u>

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

CITY OF CHEHALIS
Statement of Fiduciary Net Assets
Fiduciary Funds
December 31, 2006

	Firemen's Pension Fund
ASSETS	
Current assets:	
Cash and cash equivalents	\$ 384,594
Short Term Investments	75,000
Total Current Assets	<u>\$ 459,594</u>
 TOTAL ASSETS	 <u>459,594</u>
 LIABILITIES	
Current Liabilities:	
Warrants and accounts payable	-
TOTAL LIABILITIES	<u>-</u>
 NET ASSETS	
Held in trust for pension benefits	459,594
TOTAL NET ASSETS	<u><u>\$ 459,594</u></u>

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

CITY OF CHEHALIS
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
For the year ended December 31, 2006

	Firemen's Pension Fund
ADDITIONS	
Fire Insurance Premium Tax	\$ 9,635
Investment interest	73,414
Total Additions	<u>83,049</u>
DEDUCTIONS	
Retired Pension Benefits	<u>8,025</u>
Total Deductions	<u>8,025</u>
Change in net assets	75,024
Total net assets - Beginning	<u>384,570</u>
Total net assets - Ending	<u><u>\$ 459,594</u></u>

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

CITY OF CHEHALIS
NOTES TO FINANCIAL STATEMENTS
December 31, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Chehalis have been prepared in conformity with the accounting practices prescribed or permitted by the State Auditor's Office of the State of Washington, which is an other comprehensive basis of accounting. As more fully described in Note 15 A, the City did not fully implement Governmental Accounting Standards Board (GASB) Statement 34 for the 2006 reporting period. The GASB is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The significant accounting policies followed by the City are described below.

A. Reporting Entity

The City of Chehalis was incorporated on September 22, 1890, and operates under the laws of the State of Washington applicable to a non-charter code city with a council-manager form of government.

The City is a general purpose government and provides public safety, fire prevention, parks and recreation, water supply/treatment/distribution, sewage collection/treatment, housing rehabilitation/rental, planning and zoning, judicial administration, and general administration services.

The combined financial statements include the financial position and results of operations of all funds that are controlled by or dependent on the City. The combined financial statements also include the assets and liabilities of all funds for which the City has a custodial or trust responsibility; furthermore, the City has no component units to report in these financial statements.

B. Fund Financial Statements

Fund financial statements are provided for governmental funds, proprietary funds and fiduciary funds. Major individual government funds and major enterprise funds are reported as separate columns in the fund financial statements.

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

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Grant revenue is recognized for cost reimbursement grants when the expenditures occur in accordance with GASB Statement 1. When the expenditure is incurred, grant revenue is considered to have been earned and recognized as revenue.

The City reports the following major governmental funds:

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

The **Public Facilities Reserve Fund** accounts for Local Real Estate Excise Tax revenues and other monies set aside for capital improvements.

The City reports the following major proprietary funds:

The **Garbage Fund** provides solid waste collection services through a contract with a solid waste hauling firm. The utility's operations are self-supported through user charges.

The **Wastewater Fund** operates and maintains a treatment plant for collecting and treating wastewater effluent in accordance with state and federal requirements. The utility's operations are self-supported through user charges.

The **Water Fund** operates and maintains a water distribution system for all residential, commercial and industrial customers. The utility's operations are self-supported through user charges.

The **Storm/Surface Water Fund** operates and maintains the City's surface water collection system. The utility's operations are self-supported through user charges.

Additionally, the City reports the following fiduciary fund:

The **Pension Trust Fund** accounts for activities of the Firemen's Pension Fund, which accumulates resources for pension benefit payments to qualified retired firefighters and qualified spouses.

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

The proprietary fund statements distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's utility are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first; unrestricted resources are then used as needed.

D. Budgetary Information

1. Scope of the Budget

Annual appropriated budgets are adopted for the general and special revenue funds and for all proprietary funds on the modified accrual basis of accounting. For governmental funds, there are no differences between the budgetary basis and generally accepted accounting principles. Budgetary accounts are integrated in fund ledgers for all budgeted funds, but the financial statements include budgetary comparisons for annually budgeted major governmental funds only. Budgets for capital projects funds are only required to be adopted at the level of the project and for fiscal periods that correspond to the lives of the projects.

Annual appropriated budgets are adopted at the fund level. This is the mandated level of control. Subsidiary revenue and expenditure ledgers are used as management control devices to compare the budgeted amounts with actual revenues and expenditures on functional, departmental, activity and account levels. Appropriations for general and special revenue funds lapse at year-end.

2. Amending the Budget

The City Manager is authorized to transfer budgeted amounts between departments within any fund and object classes within departments; however, any revisions that alter the total expenditures of a fund, or that affect the number of authorized employee positions, salary ranges, hours, or other conditions of employment must be approved by the City Council.

Budgeted expenditures include the ending fund balance. Budget amendments are made only when actual expenditures are expected to exceed the total appropriation elements (expenditures and ending fund balance).

When the City Council determines that it is in the best interest of the City to increase or decrease the appropriation for a particular fund, it may do so by ordinance approved by a simple majority.

The financial statements show both the original budget and the final authorized amounts as revised during the year.

3. Excess of Expenditures over Appropriations

For the year ended December 31, 2006, expenditures did not exceed appropriations in any fund.

4. Deficit Fund Equity

As of December 31, 2006, there were no funds with a deficit fund equity.

E. Assets, Liabilities and Equities

1. Cash and Cash Equivalents

The City pools cash resources of its various funds in order to facilitate the management of cash. Cash applicable to a particular fund is readily identifiable. The balance in the pooled cash accounts is available to meet current operating requirements. Cash in excess of current requirements is invested in various interest-bearing securities and disclosed as part of the City's investments.

It is the City's policy to invest all temporary cash surpluses. At December 31, 2006, the Treasurer was holding \$5,624,267 in checking and money market accounts, and in short-term residual investments (Category 1). This amount is classified on the balance sheet and statement of net assets as cash and cash equivalents in the various funds. The interest income on these deposits is prorated to the various funds.

For purposes of the Statement of Cash Flows, the City considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

2. Investments

In accordance with Washington State law, authorized investment purchases include certificates of deposit with financial institutions qualified by the Washington Public Deposit Protection Commission, US Treasury and Agency Securities, banker's acceptances, bonds of Washington State and any local government in Washington State, which have, at the time of purchase, one of the three highest credit ratings of a nationally recognized rating agency, repurchase agreements and the Washington State Local Government Investment Pool. The Firemen's Pension Fund is also authorized to invest in corporate bonds rated "A" or better by Standard & Poor's Corporation, or "A" or better by Moody's Bond Ratings.

On December 31, 2006, all City investments were categorized as Risk Category 1 as described in GASB Statement No. 3. The definition of Category 1 includes those investments that are insured, registered or held by the City, or its agent, in the City's name.

In compliance with GASB Statement No. 31, the City records the unrealized gains/losses on investments at year-end. For the fiscal year ended December 31, 2006, the City did not have any unrealized gains or losses on investments.

3. Receivables

Taxes receivable consists of property taxes and related interest and penalties (see Note 4).

Customer accounts receivable consists of amounts owed by private individuals or organizations for goods and services provided.

Other accounts receivable consists of authorized loans and grants for which expenditures have been made but for which reimbursement has not yet been received.

Notes and contracts receivable consists of amounts owed by private individuals for goods and services provided.

4. Amounts Due To and From Other Funds and Governments, Interfund Loans and Advances Receivable

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “due to /from other funds” (i.e. the current portion of interfund loans) or “advances to/from other funds” (i.e. the non-current portion of interfund loans). All other outstanding balances between funds are reported as “due to/from other funds.” A separate schedule of interfund loans receivable and payable is furnished in Note 10.

5. Inventories

Inventories in proprietary funds are valued by the weighted-average method, which approximates the market value. The costs of governmental fund-type inventories are recorded as expenditures when purchased.

6. Restricted Assets and Liabilities

These accounts contain resources for customer deposits and debt service. The current portion of related liabilities is shown as Payable from Restricted Assets on the statement of net assets. Specific debt service requirements are described in Note 8. The current portion of related assets is shown as Restricted Cash & Equivalents; the estimated future portion of related assets is shown as Restricted Investments.

Restricted assets of the proprietary funds are composed of the following:

Customer Deposits - Cash & Equivalents	121,370
Customer Deposits - Investments	175,000
Revenue Bonds - Cash & Equivalents	132,579
Total restricted assets	<u>428,949</u>

7. Capital Assets - (See Note 5)

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported in their respective column of the statement of net assets. Capital assets are defined by the city as assets with an initial, individual cost of more than \$5,000 and an estimated useful life of more than one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

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

Land and construction in progress are not depreciated. Property, plant and equipment of proprietary funds are depreciated using the straight line method over the following estimated useful lives:

<u>Asset</u>	<u>Years</u>
Buildings/building improvements	20-50
Utility infrastructure & other improvements	20-50
Vehicles, machinery & equipment	5-20
Computer software	3

8. Other Property and Investments - (See Note 3)

9. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. All vacation and sick pay is accrued when incurred in the proprietary fund financial statements.

City personnel policies allow vacation to be accumulated up to 384 hours and is payable upon resignation, retirement or death (subject to union or employment agreements that may allow for more liberal accumulation and payment).

City personnel policies allow sick leave to be accumulated up to 720 hours. 100% of sick leave is payable upon termination of service, if certain requirements are met.

For the proprietary funds, the total accrued vacation and sick leave payable at termination of employment as of December 31, 2006 has been accrued in the financial statements. For the governmental funds, the accrued vacation and sick leave payable estimated to be paid within 60 days after December 31, 2006 has been accrued as a liability in the financial statements.

10. Other Current Liabilities

Other current liabilities at December 31, 2006 consist of the liability for trust funds held by the City and other miscellaneous liabilities.

11. Long-term Debt - (See Note 8)

12. Deferred Revenues

This account includes amounts recognized as receivables but not revenues in governmental funds because the revenue recognition criteria have not been met.

13. Fund Reserves and Designations

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

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

There have been no material violations of finance-related legal or contractual provisions in any of the funds of the City.

NOTE 3 - DEPOSITS AND INVESTMENTS

Deposits

The City's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (WPDPC).

Investments

As of December 31, 2006, the City had the following investments:

Sterling Bank CD	113,976
Venture Bank CD	1,133,605
US Bank notes and bonds	3,065,406
Total investments	<u><u>4,312,987</u></u>

NOTE 4 - PROPERTY TAXES

The Lewis County Treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Collections made by the County on behalf of the City are distributed after the end of each month.

The Property Tax Calendar is as follows:

January 1	Taxes are levied and become an enforceable lien against properties.
February 14	Tax bills are mailed.
April 30	First of two equal installment payments is due.
May 31	Assessed value of property established for next year's levy at 100% of market value
October 31	Second installment payment is due.

Property taxes are recorded as a receivable when levied, offset by deferred revenue. During the year, property tax revenues are recognized when cash is collected. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible.

The City's regular levy for 2006 was \$2.493 per \$1,000 on an assessed valuation of \$9,042,513 for a total regular levy of \$1,084,490.

The City also has a special levy for Emergency Medical Services. The special levy for 2006 was \$0.4740 per \$1,000 on an assessed valuation of \$9,042,513 for a total special levy of \$206,000.

Washington State Constitution and Washington State law, RCW 84.55.010, limit the rate.

NOTE 5 – CAPITAL ASSETS

A. Governmental Fund Capital Assets

Governmental fund capital assets that are infrastructure assets (such as roads, bridges, curbs, and sidewalks) are considered public property and are not accounted for in the City's books or in the following schedule.

The following schedule provides a summary of the changes in the governmental funds' capital assets for the year ended December 31, 2006:

Governmental Fund Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated:				
Land	\$ 2,171,700	\$ 278,100	\$ -	\$ 2,449,800
Total capital assets not being depreciated	\$ 2,171,700	\$ 278,100	\$ -	\$ 2,449,800
Other capital assets:				
Buildings	\$ 2,340,166	\$ -	\$ -	\$ 2,340,166
Other improvements	799,185	131,173	-	930,358
Equipment	3,339,406	121,416	-	3,460,822
Total other capital assets	\$ 6,478,757	\$ 252,589	\$ -	\$ 6,731,346
Less accumulated depreciation	(3,704,626)	(402,227)		(4,106,853)
Other capital assets, net	\$ 2,774,131	\$ (149,638)		\$ 2,624,493
TOTAL CAPITAL ASSETS, NET	\$ 4,945,831	\$ 128,462	\$ -	\$ 5,074,293

* Depreciation expense was calculated for functions as follows:

General government	\$ 97,951
Security of persons & property	185,561
Transportation	22,990
Culture & recreation	<u>38,236</u>
Total	<u>\$ 344,738</u>

Effective January 1, 2006, the parking fund (a proprietary fund in 2005) was closed out, and the fund's net assets were transferred into the City's general fund. The assets transferred included land with a cost of \$278,100 and other improvements with a cost of \$78,586 and accumulated depreciation of \$66,142. The transfer of these assets is included in the reported increases in the above table and in the reported decreases in the proprietary funds table below.

B. Proprietary Fund Capital Assets

Capital assets of the proprietary funds are capitalized in their respective statements of net assets. The following schedule provides a summary of the changes in the proprietary funds' capital assets for the year ended December 31, 2006:

Proprietary Fund Capital Assets	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated:				
Land	\$ 4,876,565	\$ -	\$ (643,897)	\$ 4,232,668
Construction in progress	19,729,775	18,937,659	(4,290,218)	34,377,216
Total capital assets not being depreciated	<u>\$ 24,606,340</u>	<u>\$ 18,937,659</u>	<u>\$ (4,934,115)</u>	<u>\$ 38,609,884</u>
Other capital assets:				
Buildings	\$ 4,054,183	\$ 3,377,007	\$ -	\$ 7,431,190
Other improvements	29,516,925	412,873	(178,042)	29,751,756
Equipment	3,968,709	685,076	-	4,653,785
Total other capital assets	<u>\$ 37,539,817</u>	<u>\$ 4,474,956</u>	<u>\$ (178,042)</u>	<u>\$ 41,836,731</u>
Less accumulated depreciation:	(13,901,488)	(1,006,677)	66,142	(14,842,023)
Other capital assets, net	<u>\$ 23,638,329</u>	<u>\$ 3,468,279</u>	<u>\$ (111,900)</u>	<u>\$ 26,994,708</u>
TOTAL CAPITAL ASSETS, NET	<u>\$ 48,244,669</u>	<u>\$ 22,405,938</u>	<u>\$ (5,046,015)</u>	<u>\$ 65,604,592</u>

* Depreciation expense was charged to functions as follows:

Wastewater	\$ 736,940
Water	263,551
Storm drain	6,186
Total	<u>\$ 1,006,677</u>

NOTE 6 - PENSION PLANS

Substantially all of The City of Chehalis' full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia, WA 98504-8380. The following disclosures are made pursuant to GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*.

A. Public Employees' Retirement System (PERS) Plans 1, 2 and 3

Plan Description

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/defined contribution plan. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees (not in national higher education retirement programs); judges of district and municipal courts; and employees of local governments. PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3. PERS participants joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the average final compensation per year of service, capped at 60 percent. The average final compensation is based on the greatest compensation during any 24 eligible consecutive compensation months. If qualified, after reaching the age of 66 a cost-of-living allowance is granted based on years of service credit and is capped at 3 percent annually.

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at 1 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 3 members become eligible for retirement if they have: at least ten years of service; or five years including twelve months that were earned after age 54; or five service credit years earned in PERS Plan 2 prior to June 1, 2003. Plan 3 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and Plan 3 provides the same cost-of-living allowance as Plan 2. The defined contribution portion can be distributed in accordance with an option selected by the member, either as a lump sum or pursuant to other options authorized by the Employee Retirement Benefits Board.

There are 1,168 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2005:

Retirees and Beneficiaries Receiving Benefits	68,609
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	22,657
Active Plan Members Vested	104,574
Active Plan Members Nonvested	51,004
Total	246,754

Funding Policy

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and 7.5 percent for state government elected officers. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. PERS Plan 3 defined contribution is a non-contributing plan for employers. Employees who participate in the defined contribution portion of PERS Plan 3 do not contribute to the defined benefit portion of PERS Plan 3. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2006, were as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	3.69%	3.69%	3.69%
Employee	6.00%	3.50%	***

* The employer rates include the employer administrative expense fee currently set at 0.19%.

** Plan 3 defined benefit portion only.

*** Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

Both the City of Chehalis and the employees made the required contributions. The City of Chehalis' required contributions for the years ending December 31 were as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
2006	\$ 5,305	\$ 80,144	\$ 7,897
2005	\$ 3,317	\$ 46,137	\$ 4,598
2004	\$ 9,199	\$ 28,424	\$ 9,771

B. Law Enforcement Officers' And Fire Fighters' Retirement System (LEOFF) Plans 1 and 2

Plan Description

LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. Membership in the system includes all full-time, fully compensated, local law enforcement officers and firefighters. LEOFF is comprised primarily of non-state employees, with the exception of the Department of Fish and Wildlife enforcement officers, who were first included prospectively effective July 27, 2003. LEOFF participants who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 are Plan 2 members. Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature for the LEOFF Plan 2 retirement plan. Effective January 1, 2003 firefighter emergency medical technicians (EMTs) may transfer PERS Plan 1 or Plan 2 service credit to LEOFF Plan 2 if while employed for the city, town, county or district, the EMT's job was relocated to a fire department from another city, town, county or district. LEOFF defined benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays the remainder through state legislative appropriations. LEOFF retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50. The benefit per year of service calculated as a percent of final average salary is as follows:

Term of Service	Percent of Final Average Salary
20 or more years	2.0%
10 but less than 20 years	1.5%
5 but less than 10 years	1.0%

The final average salary is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last 10 years of service. If membership was established in LEOFF after February 18, 1974, the service retirement benefit is capped at 60 percent of final average salary. A cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index).

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 50 with 20 years of service, or at the age of 53 with five years of service, with an allowance of 2 percent of the final average salary per year of service. The final average salary is based on the highest consecutive 60 months. Plan 2 retirements prior to the age of 53 are reduced 3 percent for each year that the benefit commences prior to age 53. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

There are 369 participating employers in LEOFF. Membership in LEOFF consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2004:

Retirees and Beneficiaries Receiving Benefits	8,723
Terminated Plan Members Entitled To But Not Yet Receiving Benefits	577
Active Plan Members Vested	12,348
Active Plan Members Nonvested	3,543
Total	25,191

Funding Policy

Starting on July 1, 2000, Plan 1 employers and employees will contribute zero percent as long as the plan remains fully funded. Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plan. Plan 2 employers and employees are required to pay at the level adopted by the Department of Retirement Systems in accordance with Chapter 41.45 RCW. All employers are required to contribute at the level required by state law. The Legislature, by means of a special funding arrangement, appropriated money from the state General Fund to supplement the current service liability and fund the prior service costs of Plan 2 in accordance with the requirements of the Pension Funding Council. However, this special funding situation is not mandated by the state constitution and this funding requirement could be returned to the employers by a change of statute. The methods used to determine the contribution rates are established under state statute in accordance with RCW chapters 41.26 and 41.45.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2006, were as follows:

	LEOFF Plan 1	LEOFF Plan 2
Employer*	0.18%	4.90%
Employee	0.00%	7.85%
State	n/a	2.03%

*The employer rates include the employer administrative expense fee currently set at 0.18%.

Both the City of Chehalis and the employees made the required contributions. The City of Chehalis' required contributions for the years ending December 31 were as follows:

	LEOFF Plan 1	LEOFF Plan 2
2006	\$ 165	\$ 84,389
2005	\$ 284	\$ 65,435
2004	\$ 392	\$ 130,575

C. Local Government Pension and Other Employee Benefit Trust Funds

The City of Chehalis is the administrator of a Firemen's Pension Retirement system. This system is a closed system in that the membership is limited to firefighters employed prior to October 1, 1977. This system is a defined benefit plan, and is shown as a trust fund in the financial reports of the city. There are only two survivors in the system and no current employees.

No actuarial study has been done, as the expense for such cannot be justified. Below is a schedule that shows the annual retirement pension payments. Total financial responsibility for the retirees is less than \$40,000 annually.

	Firemen's Pension Plan
2006	\$ 8,025
2005	\$ 4,198
2004	\$ 4,079

NOTE 7 - RISK MANAGEMENT

The City of Chehalis is a member of the Washington Cities Insurance Authority (WCIA).

Utilizing Chapter 48.62 RCW (self-insurance regulation) and Chapter 39.34 RCW (Interlocal Cooperation Act), nine cities originally formed WCIA on January 1, 1981. WCIA was created for the purpose of providing a pooling mechanism for jointly purchasing insurance, jointly self-insuring, and / or jointly contracting for risk management services. WCIA has a total of 121 Members.

New members initially contract for a three-year term, and thereafter automatically renew on an annual basis. A one-year withdrawal notice is required before membership can be terminated. Termination does not relieve a former member from its unresolved loss history incurred during membership.

Liability coverage is written on an occurrence basis, without deductibles. Coverage includes general, automobile, police, public officials' errors or omissions, stop gap, and employee benefits liability. Limits are \$3 million per occurrence self-insured layer, and \$12 million per occurrence in the re-insured excess layer with no annual aggregate except \$10 million per member for public officials errors and omissions. The excess layer is insured by the purchase of reinsurance and insurance. Total limits are \$15 million per occurrence. The Board of Directors determines the limits and terms of coverage annually.

Insurance coverage for property, automobile physical damage, fidelity, inland marine, and boiler and machinery are purchased on a group basis. Various deductibles apply by type of coverage. Property insurance and auto physical damage are self-funded from the members' deductible to \$500,000, for all perils other than flood and earthquake, and insured above that amount by the purchase of reinsurance.

In-house services include risk management consultation, loss control field services, claims and litigation administration, and loss analyses. WCIA contracts for the claims investigation consultants for personnel issues and land use problems, insurance brokerage, and lobbyist services.

WCIA is fully funded by its members, who make annual assessments on a prospectively rated basis, as determined by an outside, independent actuary. The assessment covers loss, loss adjustment, and administrative expenses. As outlined in the interlocal, WCIA retains the right to additionally assess the membership for any funding shortfall.

An investment committee, using investment brokers, produces additional revenue by investment of WCIA's assets in financial instruments, which comply with all State guidelines. These revenues directly offset portions of the membership's annual assessment.

A Board of Directors governs WCIA, which is comprised of one designated representative from each member. The Board elects an Executive Committee and appoints a Treasurer to provide general policy direction for the organization. The WCIA Executive Director reports to the Executive Committee and is responsible for conducting the day to day operations of WCIA.

NOTE 8 - LONG-TERM DEBT AND LEASES

A. Long-term Debt

The City periodically issues revenue bonds, general obligation bonds, promissory notes and other loans for the acquisition and construction of land, buildings, infrastructure and equipment. General obligation bonds and promissory notes have also been issued for general government activities and are repaid from the applicable sources. The revenue bonds are repaid by utility revenues generated in the appropriate proprietary fund. The City is also liable for loans that were entered into for the construction and rehabilitation of the City's buildings and infrastructure. These loans are considered obligations of the applicable proprietary fund and are being repaid with utility revenue sources. At December 31, 2006, there were no general obligation bonds outstanding.

Notes Payable

Notes payable outstanding as of December 31, 2006 consist of the following:

	<u>Principal Balance</u>
1. In 2003, the City issued a \$421,000 promissory note with a bank for the purchase of a new fire truck. Terms of the note require semi-annual payments of \$35,379, including interest at a rate of 4.25% per annum. The note matures in 2010 and is accounted for in the City's governmental funds.	\$ 255,837
2. In 2003, the City issued a \$785,126 promissory note to an individual for the acquisition of land to be used for the City's new wastewater treatment plant. The terms of the note, which is included in the proprietary wastewater fund, require semi-annual payments of \$55,242, including interest at a rate of 7.0% per annum. The note matures in 2013.	569,147
3. In 2005, the City issued a \$2.3 million promissory note with a bank. \$1.3 million of this note was used to acquire buildings for general governmental purposes and is accounted for in the City's governmental funds. The remaining \$1 million was used to pay for improvements to wastewater treatment property and is recorded in the City's proprietary wastewater fund. Terms of the note require semi-annual payments of interest only at a rate of 4.5% per annum, and the entire note is to be paid in full in December 2007.	<u>2,300,000</u>
Total notes payable	<u>\$3,124,984</u>

Notes payable activity for the year ended December 31, 2006 is summarized as follows:

	Balance, Beginning of Year	Additions	Retirements	Balance, End of Year	Amounts Due Within One Year
<u>Governmental Funds:</u>					
Note payable--fire truck	\$ 315,227	\$ -	\$ (59,390)	\$ 255,837	\$ 60,428
Note payable--bank	1,300,000	-	-	1,300,000	1,300,000
Totals--governmental funds	<u>1,615,227</u>	<u>-</u>	<u>(59,390)</u>	<u>1,555,837</u>	<u>1,360,428</u>
<u>Proprietary Funds:</u>					
Note payable--individual	636,248	-	(67,101)	569,147	71,881
Note payable--bank	1,000,000	-	-	1,000,000	1,000,000
Totals--proprietary funds	<u>1,636,248</u>	<u>-</u>	<u>(67,101)</u>	<u>1,569,147</u>	<u>1,071,881</u>
Total notes payable	<u>\$ 3,251,475</u>	<u>\$ -</u>	<u>\$ (126,491)</u>	<u>\$ 3,124,984</u>	<u>\$ 2,432,309</u>

The annual debt service requirements to maturity for notes payable as of December 31, 2006 are as follows:

Year Ending December 31	Principal	Interest
2007	\$ 2,432,309	\$ 157,362
2008	140,024	41,218
2009	148,247	32,995
2010	154,982	24,254
2011	94,653	15,831
2012 - 2016	154,769	10,958
Totals	<u>\$ 3,124,984</u>	<u>\$ 282,618</u>

Revenue Bonds Payable

The revenue bonds were originally issued in 1979 in order to pay for water and sewer improvement projects. The bonds, which mature in 2019, are recorded in the City's proprietary water fund. The bonds require semi-annual payments of principal, as specified in the bond agreement's debt service schedule, plus interest at 5.0% per annum.

Revenue bonds payable activity for the year ended December 31, 2006 is summarized as follows:

	Balance, Beginning of Year	Additions	Retirements	Balance, End of Year	Amounts Due Within One Year
Revenue bonds	<u>\$ 253,000</u>	<u>\$ -</u>	<u>\$ (12,000)</u>	<u>\$ 241,000</u>	<u>\$ 14,000</u>

The annual debt service requirements to maturity for revenue bonds payable as of December 31, 2006 are as follows:

Year Ending December 31	Principal	Interest
2007	\$ 14,000	\$ 11,875
2008	14,000	11,175
2009	14,000	10,475
2010	16,000	9,750
2011	16,000	8,950
2012 - 2016	95,000	31,600
2017 - 2021	72,000	6,600
Totals	<u>\$ 241,000</u>	<u>\$ 90,425</u>

Due to Other Governments Payable

Due to other governments payable consists of several federal and state program loans awarded to the City over the last several years for various construction, rehabilitation and upgrade projects associated with the City's wastewater treatment plant, sewer system and drinking water system. Under these programs, the City draws down funds for reimbursement of qualifying costs incurred up to the total loan amount awarded. At December 31, 2006, due to other governments payable consists of the following loans:

Loan Description/Purpose	Total Loan Awarded	Total Draws to 12/31/2006	Interest Rate	Maturity Date
Public Works Trust Fund Loans:				
PWTF #1: Sewer System Rehabilitation	\$ 1,278,533	\$ 1,278,533	1.0%	2010
PWTF #2: Rehabilitation Program	845,213	845,213	1.0%	2012

State Revolving Fund Loans--Department of Ecology:

SRFL #1: Wastewater treatment poplar tree plantation	2,819,263	2,819,263	1.5%	2024
SRFL #2: Wastewater treatment plant design	323,436	323,436	1.5%	2023
SRFL #3: Wastewater treatment plant construction	32,572,175	26,787,318	0.0%	2027

Drinking Water State Revolving Fund Loan--Department of Ecology:

SRFL #4: Water treatment residuals retention basin	939,797	841,996	2.5%	2020
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Due to other governments payable activity for the year ended December 31, 2006 is summarized as follows--

	Balance, Beginning of Year	Additions	Retirements	Balance, End of Year	Amounts Due Within One Year
PWTF #1	\$ 145,905	\$ -	\$ (29,181)	\$ 116,724	\$ 29,181
PWTF #2	319,698	-	(45,671)	274,027	45,671
PWTF #3	270,833	-	(270,833)	-	-
SRFL #1	2,680,607		(126,680)	2,553,927	128,594
SRFL #2	308,979	-	(15,066)	293,913	15,294
SRFL #3	8,269,573	18,517,745	-	26,787,318	-
SRFL #4	709,936	37,402	(47,329)	700,009	50,001
Totals	<u>\$ 12,705,531</u>	<u>\$ 18,555,147</u>	<u>\$ (534,760)</u>	<u>\$ 30,725,918</u>	<u>\$ 268,741</u>

The annual debt service requirements to maturity for due to other governments payable are as follows:

Year Ending December 31	Principal	Interest
2007	268,740	63,720
2008	1,941,281	59,548
2009	1,943,488	55,343
2010	1,945,727	51,106
2011	1,918,819	46,834
2012 - 2016	9,446,728	175,991
2017 - 2021	9,413,262	82,078
2022 - 2026	8,797,546	9,963
2027 - 2031	835,184	-
Totals	<u>\$ 36,510,775</u> *	<u>\$ 544,583</u>

* The total principal consists of the following:

Total due to other governments at December 31, 2006 \$ 30,725,918

Remaining funds to be drawn down on SRFL #3
included in debt service payment requirements

5,784,857

Total principal debt service requirements

\$ 36,510,775

In proprietary funds, unamortized debt issue costs are recorded as deferred charges, and the debt is presented net of any premium or discount; annual interest expense is accordingly decreased by the amortization of debt premiums and increased by the amortization of debt issue costs and discounts. At December 31, 2006, there were no unamortized debt issue costs, discounts or premiums.

NOTE 9 - CONTINGENCIES AND LITIGATION

The City has recorded in its financial statements all material liabilities, including an estimate for situations, which are not yet resolved, but where, based on available information, management believes it is probable that the City will have to make payment. In the opinion of management, the City's insurance policies and/or reserves are adequate to pay all known pending claims.

The City participates in a number of federal and state assisted programs. These grants are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. City management believes such disallowances, if any, will be immaterial.

NOTE 10 - INTERFUND BALANCES AND TRANSFERS

A. Interfund Balances

There were no interfund receivable or payable balances at December 31, 2006.

B. Interfund Transfers

Interfund transfers for the year ended December 31, 2006 were as follows:

Transfers To	Transfers From	Amount	Purpose
1. General Fund	Parking Fund	\$ 31,554	Close parking fund to general fund
2. Real Estate Excise Tax Funds	Public Facilities Reserve Fund	758,234	Establish real estate excise tax funds
3. Automotive Equipment Reserve	General Fund	83,500	Increase equipment reserves
4. Public Facilities Reserve Fund	Real Estate Excise Tax Funds	503,750	Increase capital reserves
			Payment of loan interest on behalf of
5. Wastewater Fund	Public Facilities Reserve Fund	23,686	Wastewater Fund
General Fund, CDBG Fund, HUD Block Grant Fund, 2nd Quarter REET Fund, Wastewater	CDBG Fund, First Quarter REET Fund and Wastewater Fund		Total transfers between funds due to
6. Fund	and Water Fund	643,375	reallocation of investment funds
		<u>\$ 2,044,099</u>	
Total interfund transfers			

During 2006, there was an immaterial difference between transfers to other funds and transfers from other funds related primarily to the reallocation of investments among the various funds.

NOTE 11 - JOINT VENTURES

Chehalis - Centralia Airport

The City of Chehalis is currently jointly participating with Lewis County in the Chehalis–Centralia Airport. The joint venture is organized under RCW 14.08.200. The Airport was originally governed jointly by the Cities of Chehalis and Centralia and by Lewis County but in 2004 Centralia withdrew. Currently the Chehalis–Centralia Airport is jointly governed by an appointed seven-member board of which the city is a member. Currently two airport board members are appointed by the city. The City and Lewis County jointly own the airport real estate. There is a deficit equity position of the airport as of December 31, 2006, primarily as result of ongoing capital development at the airport. The City made no cash contributions to the airport during 2006. Financial statements for the Chehalis–Centralia Airport can be obtained from its administrator at Airport, PO Box 1344, Chehalis, WA 98532.

NOTE 12 - POSTRETIREMENT BENEFITS OTHER THAN PENSION BENEFITS

In addition to the pension benefits described in Note 6, the City provides post-retirement health care benefits, in accordance with the Washington Law Enforcement Officers and Fire Fighters Retirement System (LEOFF) Act (RCW 41.26), to 20 retired full-time, fully compensated law enforcement officers and firefighters who established membership in the LEOFF Plan 1 Retirement System on or before September 30, 1977. Currently, 18 retirees meet those eligibility requirements.

The City of Chehalis reimburses 100 percent of the unpaid portion of validated claims for medical and hospitalization costs incurred by pre-Medicare and post-Medicare retirees. The city also pays health insurance premiums and reimburses the premium for a Medicare supplement for each retiree eligible for Medicare. This premium amount changes each January and varies per each eligible retiree.

Employer contributions are financed on a pay-as-you-go basis. Expenditures for postretirement health care benefits are recognized as retirees report claims in the Fire and Police budgets. There is no provision for estimated claims incurred but not yet reported to the city.

During the year, expenditures of \$206,909 were recognized for post-retirement health care.

NOTE 13 - OTHER DISCLOSURES

Reporting Changes

For the 2006 financial statements, the City did not fully implement GASB 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* due to turnover of the City's finance director position. The required portions of GASB 34 not implemented were the management's discussion and analysis, government-wide financial statements and infrastructure-related required information. As such, the financial statements were prepared in conformity with the accounting practices prescribed or permitted by the State Auditor's Office of the State of Washington. This is the final year that the City is allowed to report using these accounting practices. The City will have the option of fully implementing GASB 34 or converting to the cash basis of accounting for the fiscal year 2007 financial statements.

NOTE 14 – PRIOR PERIOD ADJUSTMENTS

In the process of preparing the 2006 financial statements, the City determined that three prior period corrections to the wastewater fund's net assets were necessary. Information about these prior period corrections is as follows:

1. In both 2003 and 2004, interest payable on one of the City's promissory notes was accrued as a liability, but this interest was not reversed in the next years' financial statements. Therefore, the liability and interest expense were overstated in both 2004 and in 2005, and at December 31, 2005, net assets for the wastewater fund were understated by \$79,489.
2. The City serves as an agent for a promissory note of the Port of Chehalis. The Port pays the City all amounts due on the note, and the City then issues a check for the same amount to the lender. Because the City serves as an agent for these debt payments, all receipts and disbursements related to this debt should flow through the liability account. In 2006, it was determined that amounts received in 2003 and

2004 were properly posted to the liability account, but the corresponding payments made by the City had been expensed. As a result, net assets at December 31, 2005 were understated by \$47,381.

3. In 2006, the City took a physical inventory of all capital assets on hand and reconciled the inventory with the amounts recorded in the general ledger. During this process, it was determined that the capital assets in the wastewater fund were understated at December 31, 2005 by \$26,262, and net assets had been understated by the same amount.

In summary, the total prior period correction to the wastewater fund's net assets is as follows:

Correction of prior years' interest payable	\$ 79,489
Correction of prior years' expensing of Port of Chehalis debt payments	47,381
Correction of capital asset balances	<u>26,262</u>
Total prior period corrections--wastewater fund	<u>\$153,132</u>

NOTE 15 – SUBSEQUENT EVENT

On December 3, 2007, due to extremely heavy rains within a short time-span, the City of Chehalis and Lewis County were flooded, as were adjacent counties. Both Governor Christine Gregoire and President George W. Bush declared a State of Emergency; this released Federal Emergency Management Agency (FEMA) resources to the region. Original estimates of damage to City assets come to \$3.2 million. However, due to insurance coverage and anticipated FEMA assistance, damage sustained to City assets is not expected to have a material effect upon the City's financial position.

The City's sales tax revenues were adversely affected by the flooding, as well. However, most retailers were operational in less than two weeks. Lost revenues are not expected to be material.

MCAG NO. 0487

MCAG NO. 0487

CITY OF CHEHALIS, WASHINGTON
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

NOTE 1 – BASIS OF ACCOUNTING

The schedule is prepared on the same basis of accounting as the City of Chehalis' financial statements. The City of Chehalis uses the modified GAAP option.

NOTE 2 – PROGRAM COSTS

The amounts shown as current year expenditures are only the federal portion of the program costs. Entire program costs, including the City of Chehalis' portion are more than shown.

NOTE 3 – PROGRAM INCOME

The City has loan program for low income housing assistance and for housing renovation. Under these federal programs, repayments to the City are considered program revenues (income) and loans of such funds to eligible recipients are considered expenditures. The amount of loan funds disbursed to program participants for the year was \$0. The amount of principal and interest received in loan repayments for the year was \$106,988 for the housing assistance program, and \$314,830 for the housing renovation program.

NOTE 4 – FEDERAL / STATE LOAN

The City was approved by the Washington State Department of Ecology to receive a loan totaling \$32,572,175 to build a wastewater treatment plant. Of this loan, \$26,139,743 is federal funds and \$6,432,432 is state funds. The amount listed includes the federal portion of the loan proceeds received during the year. Both current and prior year loans are also reported on the City's Schedule of Long-Term Debt.



ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

Our mission is to work in cooperation with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office has 300 employees who are located around the state to deliver our services effectively and efficiently. Approximately 65 percent of our staff are certified public accountants or hold other certifications and advanced degrees.

Our regular audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. We also perform fraud and whistleblower investigations. In addition, we have the authority to conduct performance audits of state agencies and local governments.

The results of our audits are widely distributed through a variety of reports, which are available on our Web site. We continue to refine our reporting efforts to ensure the results of our audits are useful and understandable.

We take our role as partners in accountability seriously. We provide training and technical assistance to governments and have an extensive program to coordinate audit efficiency and to ensure high-quality audits.

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