



CITY OF SALEM, VIRGINIA
COMPREHENSIVE ANNUAL FINANCIAL REPORT
YEAR ENDED JUNE 30, 2007

CITY OF SALEM, VIRGINIA



COMPREHENSIVE ANNUAL FINANCIAL REPORT YEAR ENDED JUNE 30, 2007

DEPARTMENT OF FINANCE

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INTRODUCTORY SECTION

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November 17, 2007

**The Honorable Mayor and Members of City Council
and the Citizens of Salem, Virginia**

In accordance with Section 8.9 of the Salem City Charter, we are pleased to present the City of Salem (the City) Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2007. The charter requires the City to issue an annual report on its financial position and activities and that the report be audited by an independent firm of certified public accountants. This report was prepared by the Department of Finance in conjunction with generally accepted accounting principles (GAAP) as promulgated by the Government Accounting Standards Board (GASB).

Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the City. The data as presented is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the City as measured by the financial activity of various funds and component units. All disclosures necessary to enable the reader to gain the maximum understanding of the City's financial activity have been included.

Profile of the Government

Salem is located at the southern end of the Shenandoah Valley, approximately 170 miles west of Richmond and 235 miles southwest of Washington, DC. Its position in the southeastern United States gives the City ready access, within a 500-mile radius, to nearly two-thirds of the total population of the United States. In addition, the City lies at the region's crossroads of major rail and highway systems, making it a part of the principal trade, industrial, transportation, medical, and cultural center of western Virginia.

Chartered by the Commonwealth of Virginia as a town in 1806 and as a city in 1968, Salem encompasses a land area of 14.3 square miles and operates under a council-manager form of government. The City's 2007 estimated population, 25,143, accounts for almost 8% of the population in its metropolitan statistical area (MSA), which includes the neighboring City of Roanoke and the Counties of Botetourt, Craig, Franklin and Roanoke.

The primary government provides a full range of services including general government administration, judicial administration, public safety, public works, health and welfare, parks and recreation, and community development activities. The City also owns and operates an electric distribution system, water and sewage facilities, and a civic center.

The financial reporting entity reflected in the CAFR, which is more fully described in Note 1 to the basic financial statements, conforms to the requirements of the Governmental Accounting Standards Board (GASB) Statement No. 14, as amended by GASB Statement No. 39. The accounting and reporting principles of the GASB are based on the fundamental concept that publicly elected officials are accountable to their constituents, and the financial statements should emphasize the primary government and permit financial statement users to distinguish between the primary government and its component units. There are several commissions and authorities where the City's accountability is limited to appointments to, or seats on, the respective boards. The City does not exercise financial or administrative control over these entities, so they are excluded from this report.

The City's reporting entity includes one discretely presented component unit. A component unit is a legally separate entity, which meets one of three conditions; the governing board is appointed by the primary government, the entity is fiscally dependent on the primary government, or excluding the entity could potentially result in misleading financial reporting. The discretely presented component unit is the School Board of the City of Salem. A five member appointed School Board supervises the operation of the City's school system. The school system receives significant financial support from the City. The School Board is presented in a separate column in the government-wide financial statements to emphasize that it is legally separate from the primary government and to differentiate its financial position and results of operations from that of the primary government.

The annual budget is based upon the financial policies of the City and reflects the balance between anticipated revenues and proposed expenditures. As required by City Code, the City Manager submits a recommended budget to City Council thirty days prior to the last Council meeting in May each year for the fiscal year beginning July 1st. After an extensive study process and a public hearing to receive citizen input, the City Council adopts the budget on or before June 15th.

Local Economic Condition and Outlook

Although small in area, Salem is large when looking at its economic base and that of the surrounding communities. This base consists of industrial manufacturing, medical facilities, wholesale/retail trade, agriculture, hotel and motel services, higher education, rail transportation, banking services and regional utility services.

Salem strives to provide an atmosphere and quality of life conducive to families and businesses. Over the years, Salem has been able to maintain a low unemployment rate, currently 3%, and stable property tax rates, while enjoying moderate growth. A strong educational system providing a well-educated and skilled workforce along with generally lower operating costs is a key reason why employers have chosen to relocate in Salem and the rest of the Valley. The City's effort to retain existing business and industry is an integral part of its economic development efforts. The use of public funds when appropriate to attract or expand existing businesses has paid off for Salem in terms of expanded investments and employment.

Included in the manufacturing process are hi-tech electronics, medical equipment, tires, furniture, steel and motor manufacturing, tool and die, and railroad equipment, just to name a few. The largest employers include such companies as General Electric, Hospital Corporation of America, Veterans Administration Medical Center, Carter Machinery, and Yokohama Industries. The top employers in Salem provide over 10,000 jobs to Salem's citizens and those of the surrounding valley.

The past year has seen the completion of a number of residential subdivisions along with business expansions and relocations. In the residential area, The Homeplace, The Hill and The Lawn, all high-end subdivisions, have been completed with over 134 new homes and an assessed value in excess of \$45 million. Several new subdivisions have been approved or are under construction, including Phillips Brook, North Oaks, Emory Creek and Wyndstone. Once complete, 88 new homes will be added. During the current fiscal year, 66 new homes were constructed in the City with an assessed value of \$16.5 million.

In the business and commercial market, another parcel in the Salem Commerce Park was sold during fiscal year 2007. Construction at this site is expected to begin in June 2008 and will house the corporate headquarters of a real estate company. Salem Commerce Park, with over 30 acres, is already occupied by One Beacon Insurance Company, Atlantic Mutual Insurance Company and the Waldrop Medical Office Park. When completed, the Park will provide as many as 1,500 jobs and \$100 million in assessed value, becoming a jewel in the City's efforts to provide for the future. In Salem Commerce Park, five lots are still available for commercial development as well as approximately three acres for residential development.

Several restaurants, including Henry's Memphis Barbeque, Crystal Burger, T-Bone Jacks and two Starbucks locations opened during 2007. Wendy's opened at their new building located on West Main Street and McDonalds reopened in their newly reconstructed building. A high-tech biomedical facility and Verizon Plaza opened during 2007. Other business relocations or expansions include New Millennium Steel and Alouf Aesthetics. At St. John Place Commerce Center, construction of two buildings was completed, with the third underway. Other undeveloped land is available at St. John Place Commerce Center for future development.

Fiscal year 2007 revenue performance reflected increases in business license tax of 10.1%, admissions tax of 6.2% and transient lodging tax of 4.3%. Personal property and real estate taxes were relatively level. Not being a reassessment year, real estate tax revenue grew approximately 2% as anticipated. Intergovernmental revenues increased, including funding received for state highway maintenance, Comprehensive Services Act and reimbursement from the Compensation Board. Fiscal year 2007 solidified the savings the City derived from the refunding of the City's 2002 Bonds.

As part of its fiscal year 2007 budget process, the City was again able to meet the goals of maintaining service levels to citizens, providing additional funding for employee compensation and benefits, and capital replacement and maintenance.

Accounting System and Budgetary Controls

The City has established a comprehensive internal control framework designed to both safeguard the government's assets against loss from unauthorized use or theft and to properly record and adequately document transactions in order to compile information for the presentation of the City's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement.

Currently the City utilizes a financial management system that was developed internally in conjunction with the Department of Management Information Services. The City established an Information Technology Planning Board (ITPB) charged with reviewing both current business practices and best practices in order to develop a Request for Proposal for a new Financial Management System. The goal of this project is to obtain enterprise functionality that fully utilizes technology to maximize the users' ability to retrieve data. Systems to be included are financial, payroll / human resources, budget and treasury management. City-wide needs assessment and ERP planning have been underway in the current fiscal year. Implementation will take place in three phases with the initial phase coinciding with the completion of the City's new data center, which is anticipated to be in December 2008.

The budget function is used as a management tool, including performance objectives, goals and long-range planning, as well as maintaining budgetary controls. The objective of these budgetary controls is to ensure compliance with legal provision embodied in the annual appropriated budget approved by City Council. Activities of the general fund and debt service fund are included in the annual budgetary control (that is, the level at which expenditures cannot legally exceed the appropriated amount) is established at the fund level. The government also maintains an encumbrance accounting system as one technique of accomplishing budgetary control. Encumbered amounts lapse at year-end. However, encumbrances generally are re-appropriated as part of the following year's budget.

Risk Management

The City utilizes a variety of techniques to identify and monitor risks and exposures for the City activities. Risk Management is a function of several departments under the General Government heading. The City is insured for most General Liability and Property coverage. In addition, Workmen's Compensation is covered by insurance through the Virginia Municipal Self Insurance Association. The City is self-insured for health coverage for City and School employees. Note 13 of the financial statements provides an outline of Salem's Risk Management Coverage.

Cash Management

The City uses a pooled cash concept to allow greater investment flexibility and consequently a better return on investments. Cash from all funds except those restricted for specific purposes is pooled for investment purposes with maturities planned to coincide with cash needs. Funds not immediately needed (30 days or greater) are invested in certificates of deposit or other approved investments, while funds available for periods of less than 30 days are invested with the City's lead bank as a part of its cash management program. All City funds are collateralized in accordance with the Virginia Security for Public Deposits Act or covered by Federal Depository Insurance.

Major Initiatives and Accomplishments

Salem City Council and Management are committed to making Salem a great place to live, work, and raise a family. To that end, the City and School Board work diligently to provide one of the finest school systems not only in the region but throughout the Commonwealth. Student scores both on National Testing and the Standards of Learning either meet or exceed state and national averages.

Salem works hard in the areas of economic development and is committed to creating jobs for its citizens and in generating new sources of tax revenue by strengthening and diversifying its economy. Salem Commerce Park is now under construction with three successful businesses and space for several more.

Salem continues to be active in tourism development as a means of economic development. Located at the Salem Civic Center, the Visitor's Center provides an abundance of information about local sites and events. The City continues to participate with the Roanoke Valley Convention and Visitors Bureau to promote conventions and events in the region. Events such as Salem Avalanche Baseball, Olde Salem Days, the Salem Fair, Stagg Bowl, Commonwealth Games, the Roanoke Valley Horse Show, NCAA Championship events, the Virginia Tech Memorial and many other events bring hundreds of thousands participants, spectators, and tourists to Salem and the surrounding area.

During fiscal year 2007, several capital improvement projects were completed. The new Public Safety addition with a newly enhanced E-911 Communications center, classrooms, and office space was completed. The addition almost doubled the size of the Public Safety building. The new Solid Waste Transfer Station became operational during 2007 and greatly improved the efficiency of Salem's waste disposal operations.

Spartan Field, located at Salem High School, was rebuilt from the ground up and synthetic turf added to bring it to NCAA Championship standards. As a result, Women's Division II National Championships were held there in 2007. Salem was the host site for five NCAA national championships during the past year, bringing thousands of athletes, fans and spending to Salem and the rest of the valley. Salem Stadium was also upgraded with new synthetic turf, landscaping and other amenities.

A joint partnership between Salem and the Virginia Department of Transportation was realized with the street improvement and bridge replacement project on East Main Street. Salem, in partnership with the Counties of Roanoke, Franklin and Montgomery, created the Western Virginia Regional Jail Authority and began construction on a new regional jail intended to house 800 inmates.

Blue Ridge Behavioral Healthcare, long represented as an agency fund of the City, was able to become totally self-sufficient and is no longer included in this report.

Like many businesses and other local governments Salem will soon face the retirement of the "Baby Boomer Generation". In order to effectively plan for this event the City has created a "Leadership Program" to identify and instill in the younger management staff the ethics, knowledge, education, and technical training to pass on the "Salem Way" to future leaders of the City. Currently, over 50 individuals are enrolled in this program.

Prospects for the Future

The budget for 2007-08 includes both cost-of-living and merit increase. It maintains all real and personal property tax rates. Overall the General Fund, which includes the School Division, increased by 1.4% over the amended 2006-07 Budget and meets all of the City's current requirements.

Salem's first major upgrade to its electric distribution system since the early 80's is underway. Construction continued on two new electric substations and the upgrade of existing electric substations, which will increase the reliability of the City's electric distribution system. The project is expected to be completed in the fall of 2007. Demolition of the old water plant began so construction of the new electric department service center and administrative building can begin. The City's data center will also be housed at the new building. This project is expected to be completed in the fall of 2009.

The City invested in a regional wastewater collection and treatment contract to increase the City's wastewater treatment capacity. Completion of regional plant upgrades are expected in the coming year.

The City of Salem was authorized by the State Corporation Commission to provide local exchange telecommunication services. The City has undertaken a feasibility study to evaluate the provision of a broad range of services, which may include broadband, cable, wireless, phone and other telecommunication services.

The City expects to complete the actuarial study to determine the impact of GASB 45 regulations on the City and look at recommendations for its health plan applicable to retirees. As required, implementation will occur in fiscal year 2008-09.

Lastly, Salem City Council accepted Management's recommendation to move to an annual reassessment process for real estate. This process will allow for a more even and predictable growth in real estate assessments rather than the current bi-annual method. The transition will take place in the 2007-08 fiscal year.

Independent Audit

Virginia law and the Charter of the City of Salem require that the financial statements of the City be audited by a Certified Public Accountant selected by City Council. Brown, Edwards & Company, L.L.P., has performed an annual audit of the Comprehensive Annual Financial Report. Their audit was conducted in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications for Audits of Counties, Cities and Towns* issued by the Auditor of Public Accounts of the Commonwealth of Virginia. The auditor's report, which includes their opinion on the financial statements of the City, is contained in the Financial Section of this report. Other auditor's reports are included in the Compliance Section.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) has awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Salem, Virginia, for its Comprehensive Annual Financial Report for 2006. This represents the nineteenth year that Salem has earned this distinction. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. We believe this report conforms to the Certificate of

Achievement Program requirements, and standards and are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgments

We would like to express our appreciation to the staff of the Finance department for the dedication and professionalism demonstrated daily assuring the financial integrity of the City and the preparation of this report. We would also like to express our appreciation to you, City Council, for the continued insight to bring to this City and the strong commitment you have made to its fiscal integrity and financial leadership. Lastly, we would like to express our appreciation to our independent auditing firm, Brown, Edwards & Company, L.L.P., for their cooperation and input in our efforts.

Respectfully submitted,

Forest G. Jones
City Manager

Frank P. Turk
Director of Finance

**CITY OF SALEM, VIRGINIA
DIRECTORY OF PRINCIPAL OFFICIALS
June 30, 2007**

MEMBERS OF CITY COUNCIL

Howard C. Packett Mayor
John C. Givens Vice-Mayor
John C. Clemens
Jane W. Johnson
Brian R. Foley

GENERAL CITY GOVERNMENT

Forest G. Jones City Manager
James E. Taliaferro Assistant City Manager and Clerk of Council
Frank P. Turk Director of Finance
Stephen M. Yost City Attorney
Bonnie C. McCormack City Treasurer
Linda M. Carroll Commissioner of Revenue
Thomas E. Bowers Commonwealth's Attorney
Gary Chance Crawford Clerk of Circuit Court
Roger L. Surber City Sheriff
Carolyn H. Barrett Director of Human Resources
Mark R. Waldron Director of Management Information Services
James R. Bryant Chief of Police Department
Chester G. Counts Fire Chief
Charles E. Van Allman, Jr. City Engineer
Norman M. Tyler, Jr. Director of Streets and General Maintenance
John P. Shaner Director of Parks and Recreation Department
Janis C. Augustine Library Director
Dana M. Oliver Registrar
A. K. Briele, III Director of Electric Department
Melvin B. Doughty Director of Water and Sewer Department
Wendel I. Ingram Real Estate Assessor
Charles B. Aldridge, Sr. Building Official and Zoning Administrator
James M. Fender, Jr. Director of Solid Waste Disposal
Melinda J. Payne Director of Planning and Community Development
R. Carey Harveycutter, Jr. Director of Civic Facilities

CITY OF SALEM SCHOOL DIVISION

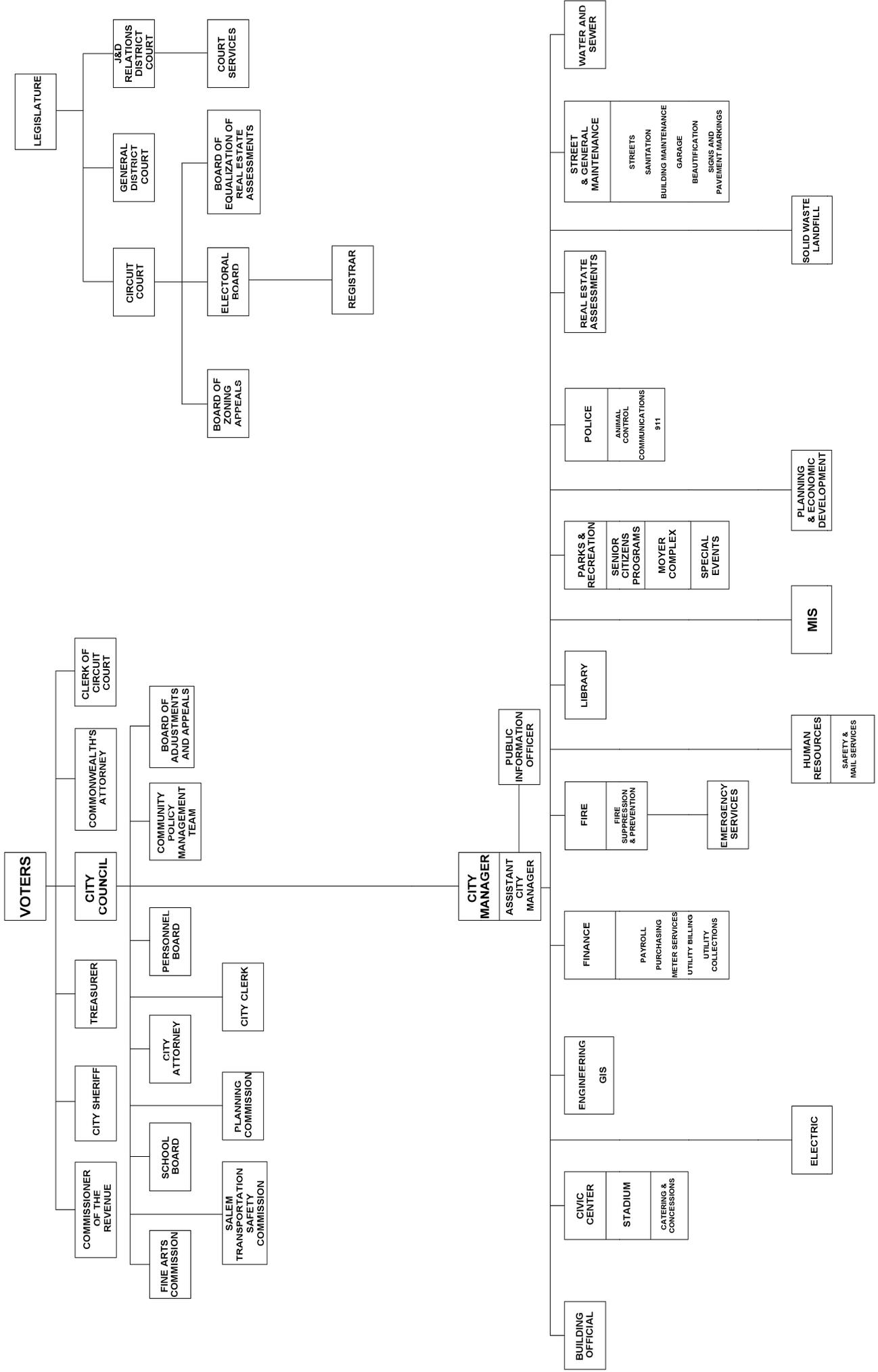
MEMBERS OF SCHOOL BOARD

Sally W. Southard Chairman
C. Wayne Adkins Vice-Chairman
James L. Chisom
Cindy W. Neathawk
William Sinkler

SCHOOL ADMINISTRATION

Dr. H. Alan Seibert Superintendent of Schools
Michael A. Bryant Assistant Superintendent
Frank P. Turk Director of Finance
Joseph T. Coleman Director of Assessment and Technology
Michael R. Crew Director of Business Services
Russell L. Holladay Director of Personnel Services
Joe G. Kirby, III Director of Secondary Instruction
Dr. Lewis D. Romano Director of Student Services
Diane D. Washenberger Director of Elementary Instruction

CITY OF SALEM, VIRGINIA ORGANIZATIONAL CHART



Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Salem
Virginia

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2006

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

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FINANCIAL SECTION

INDEPENDENT AUDITOR'S REPORT

To the Honorable Members of the City Council
City of Salem, Virginia
Salem, Virginia

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salem, Virginia 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 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications for Audits of Counties, Cities, and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia. 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.

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, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salem, Virginia, as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof and the budgetary comparison for the general fund 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 November 17, 2006, on our consideration of the City's internal control over financial reporting and 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 supplementary information on pages 3a and 41, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The introductory section, combining and individual nonmajor fund statements, and statistical section are presented for purposes of additional analysis and are not a required part of the 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 also not a required part of the basic financial statements of the City. The combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 17, 2006

**CITY OF SALEM, VIRGINIA
MANAGEMENT'S DISCUSSION AND ANALYSIS
Year Ended June 30, 2007**

The following discussion and analysis of the City of Salem's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2007. It should be read in conjunction with the transmittal letter and the City's basic financial statements.

FINANCIAL HIGHLIGHTS

- The total assets of the City of Salem Primary Government exceeded its liabilities as of June 30, 2007 by \$139.1 million (*net assets*). Of this amount, \$127.5 million is invested in capital assets and \$11.6 million is unrestricted.
- During the year, the City's governmental activities reflect an increase in net assets of \$1.1 million. Net assets of governmental activities totaled \$76.7 million at June 30, 2007.
- The business-type activities net assets at June 30, 2007 totaled \$62.4 million, an increase of \$3.6 million from the June 30, 2006 balance. Of this amount, approximately \$20.8 million is unrestricted.
- Component unit net assets decreased by \$0.6 million to \$42.4 million. Of this amount, \$1.8 million is unrestricted while \$40.6 million is invested in capital assets.
- At the end of the current fiscal year, undesignated fund balance for the general fund was approximately \$5.9 million or 9.8% of fiscal year 2007 general fund revenues. The City Council has stated its intent to increase the undesignated general fund balance to a minimum of 15.0% of general fund revenues.

OVERVIEW OF THE FINANCIAL STATEMENTS

Our discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's financial statements present two types of statements, each with a different snapshot of the City's finances. The focus is on both the City as a whole (government-wide) and the fund financial statements. The government-wide financial statements provide both short-term and long-term information about the City's overall financial status. The fund financials focus on the individual parts of City government, reporting the City's operations in more detail than the government-wide statements, which present a longer-term view. Presentation of both perspectives provides the user a broader overview, enhances the basis for comparisons, and better reflects the City's accountability.

Government-Wide Financial Statements

The government-wide financial statements include the Statement of Net Assets and the Statement of Activities. These statements provide information about the City as a whole using the accrual basis of accounting, which is the method used by most private-sector enterprises. All current year revenues and expenses are reported in the Statement of Activities regardless of when cash is received or paid. These statements allow readers to answer the question, "Is the City's financial position, as a whole, better or worse as a result of the year's activities?"

One of the main goals of these two statements is to report the City's net assets and changes that affected net assets during the fiscal year. The change in the City's net assets, the difference between assets and liabilities, is one way to measure the City's financial health, or financial position. Increases or decreases in net assets are indicators of whether the City's financial health is improving or deteriorating. Other non-financial factors, such as changes in the City's property tax base and the condition of the City's infrastructure should also be considered in assessing the overall financial health of the City.

In the Statement of Net Assets and the Statement of Activities, the City's fund-based activity is classified as follows:

Governmental activities – Most of the City's basic services are reported here, including general government, judicial administration, public safety, public works, health and welfare, education, parks and recreation, and community development departments. Property taxes, other local taxes, and federal and state grants finance most of these activities.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Business-type activities – The City's Electric Distribution System, Water and Sewage Systems, Civic Center, and Catering and Concessions are reported here as the City charges a fee to customers designed to cover all or most of the cost of services it provides.

Component unit – The City includes a discretely presented component unit in this report, the Salem School Division. Although legally separate, the component unit is important because the City of Salem is financially accountable for it.

Fund Financial Statements

The fund financial statements begin on page 33 and provide detailed information about the most significant funds, not the City as a whole. The City has three types of funds.

Governmental funds – Most of the City's basic services are included in governmental funds. Fund-based statements for these funds focus on how resources flow into and out of those funds and the balances left at year end that are available for future spending. These funds are reported on the modified accrual basis of accounting, which measures cash and other liquid assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term overview that helps the reader determine the financial resources that can be spent in the near future to finance the City's programs. The differences between governmental activities as reported in the government-wide and fund financial statements are reconciled in Exhibits 3 and 4 on pages 33 and 34.

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, like the government-wide statements, utilize the accrual basis of accounting and their statements provide both short and long-term financial information.

The City's enterprise funds, one type of proprietary fund, are the same as the government-wide business-type activities; however, the fund financial statements provide more detail and additional information, such as cash flows. The City's enterprise funds include the Electric Distribution System, Water and Sewage Systems, Civic Center and Catering and Concessions.

Fiduciary funds – Resources held for other governments or agencies not part of the City are reported as fiduciary funds. These activities are excluded from the government-wide financial statements because the City cannot use these assets to finance its operations. The accounting used for fiduciary funds is much like that used for proprietary funds. The City accounts for assets held on behalf of the Cardinal Criminal Justice Academy and the Court-Community Corrections Program as agency funds. Agency funds are custodial in nature and do not involve measurement of results of operations.

Notes to the basic financial statements. The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found beginning on page 41 of this report.

Required supplementary information. In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City's and School Division's progress in funding its obligation to provide pension benefits to its employees. Required supplementary information can be found beginning on page 63 of this report.

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

A comparative analysis of government-wide information is as follows:

Summary of Net Assets:

The following table presents a condensed summary of net assets:

**Summary of Net Assets (as restated)
June 30, 2007 and 2006
(In Thousands)**

	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2007	2006	2007	2006	2007	2006	2007	2006
	Current and other assets	\$ 12,407	\$ 13,131	\$ 40,410	\$ 43,099	\$ 52,817	\$ 56,230	\$ 6,558
Capital assets, net	100,419	99,536	92,412	88,666	192,831	188,202	40,662	41,809
Total assets	112,826	112,667	132,822	131,765	245,648	244,432	47,220	46,842
Other liabilities	3,088	4,147	5,602	6,098	8,690	10,245	4,083	3,539
Long-term liabilities	33,017	32,917	64,816	66,908	97,833	99,825	697	577
Total liabilities	36,105	37,064	70,418	73,006	106,523	110,070	4,780	4,116
Invested in capital assets, net of related debt	85,853	88,112	41,636	36,955	127,489	125,067	40,662	41,809
Unrestricted	(9,132)	(12,509)	20,768	21,804	11,636	9,295	1,778	1,194
Total net assets	\$ 76,721	\$ 75,603	\$ 62,404	\$ 58,759	\$ 139,125	\$ 134,362	\$ 42,440	\$ 43,003

The City's combined net assets increased from \$134.4 million to \$139.1 million as a result of an increase in net assets of governmental activities of \$1.1 million and an increase in net assets of business type activities of \$3.6 million.

Unrestricted net assets, the portion of net assets that can be used to finance the day-to-day operations of the City, totaled \$11.6 million. Net assets invested in capital assets, net of related debt, represents the amount of capital assets owned by the City, including infrastructure, net of any outstanding debt issued to fund the asset purchase or construction. Net assets are reported as restricted when constraints on asset use are externally imposed by creditors, grantors, contributors, regulators, or are imposed by law through constitutional provisions or enabling legislation.

The net assets of governmental activities increased \$1.1 million during 2007. Significant current year activities affecting net assets include:

- Unrestricted net assets of governmental activities are negative due to the amount of debt issued for school improvements. The City assumes all debt issued for school improvements, while the School Division records the related asset. As of June 30, 2007, approximately \$19 million of bonds payable related to School Division projects were recorded as a liability of the City and reduced unrestricted net assets of governmental activities.
- General revenues including property taxes, sales tax, business and professional occupational license taxes, meals tax, state aid and interest and investment income showed growth from the prior year.
- Governmental activities expenses increased \$2.7 million or 4.6% from the prior year due to the increased contribution to the City of Salem Schools, which was \$829,000 higher than the previous year. In addition, public works expenses were approximately \$1.0 million higher than the previous fiscal year.
- Capital grants and contributions declined from the previous year. In fiscal year 2006, the Virginia Department of Transportation contributed assets to the City of approximately \$6.4 million for the East Main Street transportation project. This project was completed in the current year and \$1.1 million in assets were contributed by the Virginia Department of Transportation.

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

The net assets of business-type activities increased approximately \$3.6 million during 2007. Significant current year activities affecting net assets include:

- Water and sewer rates increased approximately 15% and 20%, respectively, to cover increasing costs of operation. Charges for services for the water and sewage fund increased approximately \$1.2 million. Electricity rates also increased and are reflected in the 6% increase in charges for services. Investment earnings were higher than the prior year due to higher investment yields and the investment of the 2006 bond proceeds.
- Net transfers of \$495,995 include the following amounts transferred from business-type activities to governmental activities: a payment in lieu of taxes of \$1,265,000, the transfer of capital assets with a net value of \$87,013 and the transfer of \$318,000 to fund capital projects. Governmental activities provided operational support to the Civic Center in the amount of \$1,174,018.

School Division revenues increased \$3.3 million from the prior year and totaled \$40.0 million while expenses, including depreciation, increased by \$1.4 million to \$40.6. Higher salary and benefit costs system-wide contributed to this increase. Federal grant program expenses also increased, while related operating grants and contributions remained level with the prior year. State aid was higher than the previous year due to an increase in per pupil amounts resulting from SOQ rebenchmarking. Despite the increase in state aid and contributions from the City of Salem, net assets decreased \$0.5 million.

Summary of Changes in Net Assets:

The following tables show the revenues of the government:

**Summary of Changes in Net Assets (as restated)
For the Years Ended June 30, 2007 and 2006
(In Thousands)**

	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2007	2006	2007	2006	2007	2006	2007	2006
Revenues								
<i>Program Revenues:</i>								
Charges for services	\$ 4,577	\$ 3,586	\$ 42,145	\$ 39,014	\$ 46,722	\$ 42,600	\$ 1,570	\$ 1,477
Operating grants and contributions	7,024	6,038	-	-	7,024	6,038	6,560	5,595
Capital grants and contributions	1,169	6,393	-	-	1,169	6,393	-	-
<i>General Revenues:</i>								
Property taxes	27,607	27,162	-	-	27,607	27,162	-	-
Local portion of state sales tax	5,712	5,635	-	-	5,712	5,635	-	-
Business and professional occupational license taxes	4,258	3,867	-	-	4,258	3,867	-	-
Utility taxes	1,229	1,372	-	-	1,229	1,372	-	-
Meals tax	2,397	2,351	-	-	2,397	2,351	-	-
Other taxes	2,700	2,625	-	-	2,700	2,625	-	-
Intergovernmental revenue not restricted	3,879	3,524	-	-	3,879	3,524	-	-
State aid unrestricted	-	-	-	-	-	-	14,318	12,895
Interest and investment income	789	556	929	271	1,718	827	-	-
Other	279	619	27	-	306	619	450	413
Payments from Salem City	-	-	-	-	-	-	17,095	16,266
Total Revenues	\$ 61,620	\$ 63,728	\$ 43,101	\$ 39,285	\$ 104,721	\$ 103,013	\$ 39,993	\$ 36,646

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

The property tax classification, which comprises 44.8% of total revenue generated by governmental activities, includes real estate tax, the local portion of personal property tax, machinery and tools tax and public service corporation taxes. Real estate tax revenue, the largest source of revenue for the City, totaled approximately \$18.7 million. Fiscal year 2007 was not a reassessment year and the assessed value of real property in the City increased approximately 2% primarily from new construction.

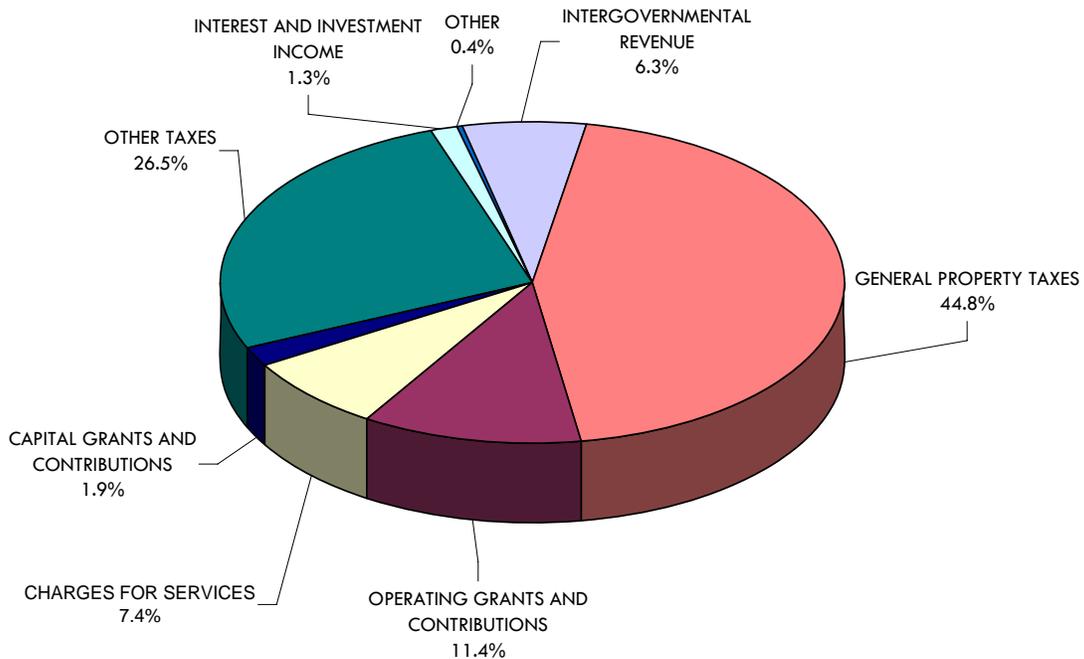
The Commonwealth share of personal property under Personal Property Tax Relief Act totaled \$2.6 million and is included in the intergovernmental revenue category. Personal property tax revenue, including the Commonwealth share, totaled \$8.2 million, reflecting a 1.7% increase from the prior year.

Operating grants and contributions comprise approximately 11.4% of governmental activities revenue, reflecting an increase of almost \$1 million compared to the previous year. Street maintenance funds, reimbursement for social service programs, funding received under House Bill 599 for law enforcement, and reimbursement for shared expenses of the constitutional officers increased from the prior year.

Charges for services include items such as fines, court fees, inspection fees, garbage collection fees along with recreation and other program-based fees and generated 7.4% of governmental activities revenue.

Revenues generated for governmental activities are presented below by category:

REVENUES



**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

The following tables show the expenses of the government:

**Summary of Changes in Net Assets
For the Years Ended June 30, 2007 and 2006
(In Thousands)**

Expenses	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2007	2006	2007	2006	2007	2006	2007	2006
General government	\$ 4,803	\$ 5,107	\$ -	\$ -	\$ 4,803	\$ 5,107		\$ -
Judicial administration	1,541	1,458	-	-	1,541	1,458		-
Public safety	13,870	13,547	-	-	13,870	13,547		-
Public works	13,476	12,443	-	-	13,476	12,443		-
Health and welfare	2,193	2,055	-	-	2,193	2,055		-
Education	17,095	16,266	-	-	17,095	16,266	40,556	38,177
Parks, recreation and cultural	5,796	5,240	-	-	5,796	5,240		-
Community development	1,022	933	-	-	1,022	933		-
Interest and fiscal charges	1,202	1,267	-	-	1,202	1,267		-
Electric distribution	-	-	24,219	24,692	24,219	24,692		-
Water and sewage	-	-	11,074	10,836	11,074	10,836		-
Civic Center	-	-	2,563	2,365	2,563	2,365		-
Catering and concessions	-	-	1,104	1,037	1,104	1,037		-
Total Expenses	60,998	58,316	38,960	38,930	99,958	97,246	40,556	38,177
Excess (Deficiency) before transfers	622	5,412	4,141	355	4,763	5,767	(563)	(1,531)
Transfers	496	976	(496)	(976)	-	-	-	-
Increase (Decrease) in net assets	<u>1,118</u>	<u>6,388</u>	<u>3,645</u>	<u>(621)</u>	<u>4,763</u>	<u>5,767</u>	<u>(563)</u>	<u>(1,531)</u>
Net Assets, Beginning, as reported of restatement of prior period	75,603	69,215	58,759	59,380	134,362	128,595	43,003	44,534
Net Assets, Ending	<u>\$ 76,721</u>	<u>\$ 75,603</u>	<u>\$ 62,404</u>	<u>\$ 58,759</u>	<u>\$ 139,125</u>	<u>\$ 134,362</u>	<u>\$ 42,440</u>	<u>\$ 43,003</u>

Local support of education expenses comprises 28% of governmental activities. Funding of \$17.1 million was provided to the School Division to support School operations, an increase of 5% from fiscal year 2006.

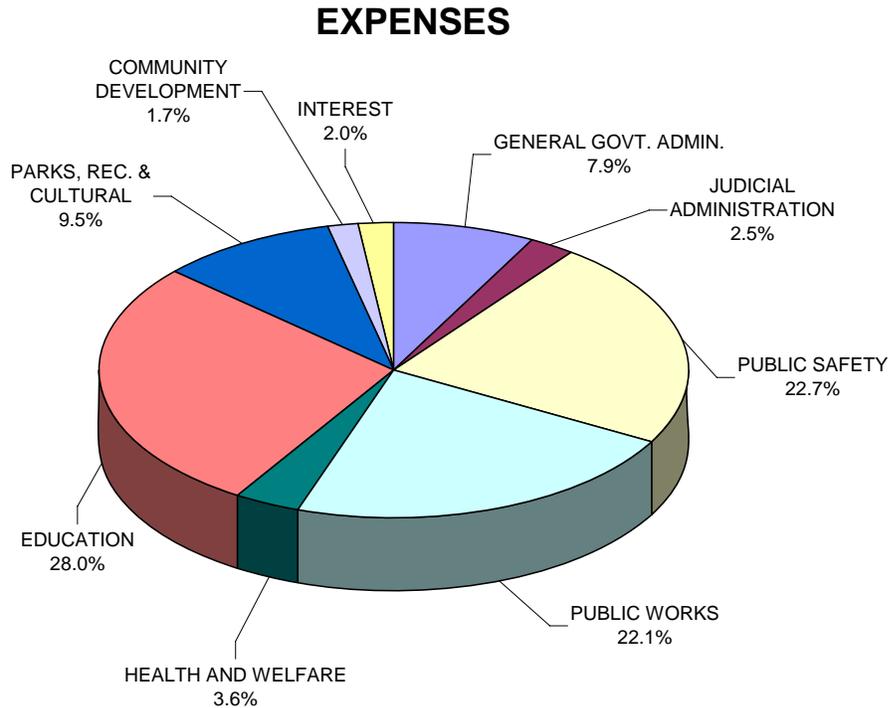
Public safety expenses comprised approximately 22.7% of governmental activities. Operations of the police and fire departments are included in this category, along with expenses of emergency medical services, Communications (E911 call center), and the cost of juvenile justice programs. Expenses for both the police and fire departments increased from the prior year largely due to increased personnel costs.

Public works and parks, recreation and cultural expenses comprised approximately 22.1% and 9.5% respectively, of governmental activities. Expenses for engineering, solid waste management, building maintenance, street paving, traffic engineering and street maintenance are included in the public works category. Public works expenses increased from the prior year due to a new contract for solid waste disposal with Waste Management Inc., which increased costs to the City. Maintenance of City parks, library expenses and expenses for City-wide recreational and athletic events are included in the parks, recreation and cultural expense category.

The Comprehensive Services Act and social services programs incurred the majority of expenses reported in the health and welfare category, which comprised 3.6% of governmental activities expenses and increased 6.7% from the prior year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Expenses of the governmental activities are shown below by functional area:



FINANCIAL ANALYSIS OF THE CITY'S FUNDS

For the fiscal year ended June 30, 2007, the governmental funds reflect a total fund balance of \$8,799,260. Approximately \$6.4 million of this amount constitutes unreserved fund balance, which is available for spending for services and capital projects. Unreserved fund balance is available to purchase capital equipment, pay self-insured claims, pay for future years' capital projects expenditures and provide for unforeseen circumstances. The remainder of fund balance is reserved for inventory and encumbrances, which indicates that it has already been committed to liquidate contracts and purchase orders outstanding at year-end.

The General Fund is the chief operating fund of the City. At the end of the current fiscal year, the general fund unreserved fund balance was \$6,547,440, while the total fund balance was \$7,904,474. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents approximately 11.5% of the total General Fund expenditures, while total fund balance represents 13.9% of that same amount.

In fiscal year 2007, fund balance of the General Fund increased by \$52,714. While revenues in several categories were slightly under budget, interest earnings during the year were higher than anticipated. Expenditures in each category were within their budget and health insurance costs were lower than expected.

Property and local taxes generated the majority of General Fund revenue, totaling approximately \$44.5 million in fiscal year 2007. Real estate taxes showed moderate growth of 2%, which was anticipated since fiscal year 2007 was not a reassessment year. Business license tax increased approximately 10% due to the reorganization of one of the City's larger taxpayers, which placed them in a different tax rate. Personal property tax revenue increased approximately 2% while machinery and tools tax increased only 1%, indicating level business investment compared to the prior year. There were no increases in the rates assigned to any of the City's real, personal property or other taxes.

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

Intergovernmental revenue is the next largest source of General Fund revenues, generating approximately \$10 million in fiscal year 2007, an increase of \$1.4 million from the prior year. Most of this revenue is received from the Commonwealth and includes personal property tax relief funds, reimbursement for social services programs, library grants, law enforcement funding received under House Bill 599 and street maintenance funds. Communications tax reform became effective January 1, 2007 and funds received from the state for this program totaled \$525,856 in the current fiscal year. Reimbursements received for street maintenance funding, the Comprehensive Services Act and the Compensation Board funding increased from the prior year.

The Capital Projects Fund balance increased \$106,429. Several large projects, including the public safety building addition, construction of the new transfer station, Salem Stadium improvements and improvements to Spartan Field were completed. \$2.5 million of the 2006 bond proceeds were reallocated and transferred to the Capital Projects Fund to cover expenditures incurred for these projects.

GENERAL FUND BUDGETARY HIGHLIGHTS

The City's budget is prepared in accordance with the *Code of Virginia*. During the year, the City amended the original budget primarily for the following purposes:

- To re-appropriate monies to pay for commitments in the form of encumbrances established prior to June 30, 2006, but not paid by that date.
- To re-appropriate grants, donations and other revenues authorized in fiscal year 2006 or earlier, but not expended or encumbered as of June 30, 2006.
- To appropriate grants, donations, and other revenues accepted or adjusted in fiscal year 2007 when official notice of approval was received.
- To appropriate the undesignated general fund balance to capital projects.
- To appropriate funds as authorized by City Council during the mid-year review process.

Below is a condensed version of the budgetary comparison of the General Fund original budget, amended budget and actual amounts for the fiscal year 2007.

Budgetary Highlights for 2007

	Original Budget	Budget As Amended	Actual
Revenues/Transfers In	\$ 58,932,674	\$ 62,074,618	\$ 61,695,164
Expenditures	54,705,332	59,624,622	57,015,109
Transfers Out	(4,627,342)	(4,627,341)	(4,627,341)
Use of Fund Balance	<u>\$ (400,000)</u>	<u>\$ (2,177,345)</u>	<u>\$ 52,714</u>

CAPITAL ASSETS

As of June 30, 2007, the City's capital assets for its governmental and business-type activities amounted to \$192.8 million net of accumulated depreciation. This investment includes land, land improvements, buildings and structures, equipment, infrastructure, historical treasures and construction in progress. The total net increase (additions less retirements and depreciation) in the City's investment in capital assets for the current fiscal year was \$4.6 million or 2.4%.

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

**Capital Assets, Net of Depreciation
June 30, 2007 and 2006
(In Millions)**

	Governmental Activities		Business-type Activities		Total Primary Government	
	2007	2006	2007	2006	2007	2006
	Land and improvements	\$ 4.8	\$ 4.5	\$ 1.3	\$ 1.3	\$ 6.1
Buildings and improvements	28.0	19.4	3.8	3.9	31.8	23.3
Equipment	5.3	4.5	2.3	2.3	7.6	6.8
Infrastructure	60.9	54.6	-	-	60.9	54.6
Construction in progress	1.4	16.5	24.7	18.2	26.1	34.7
Distribution and transmission	-	-	6.6	7.0	6.6	7.0
Utility plant	-	-	37.7	39.5	37.7	39.5
Sewage treatment contract	-	-	16.0	16.5	16.0	16.5
Total	\$ 100.4	\$ 99.5	\$ 92.4	\$ 88.7	\$ 192.8	\$ 188.2

The changes in each category of capital assets are presented in detail in note 6 to the Basic Financial Statements on page 51.

Major capital asset events during the fiscal year included the following:

- The new transfer station was put in service during the fall of 2006. The total cost of the project was \$5.35 million. The new facility has the capacity to move twice the amount of waste in half the time of the old facility. This enables transfer station employees to spend more time recovering recyclable materials.
- Construction was also completed on the addition to the Public Safety Building, which houses a communication center, administrative offices, classrooms and locker rooms for the Police Department. The addition almost doubled the size of the Public Safety Building. The total cost of the addition was \$5.5 million.
- Improvements were made at Spartan Field at a cost of \$1.3 million. Synthetic turf was installed and a new ticket booth, picnic shelter and a 950-seat grandstand with a press box were constructed. New sidewalks and landscaping were also added.
- Synthetic turf was installed at the Salem Stadium. Landscaping, storm drain improvements and the addition of concrete sidelines were included in the project, which cost approximately \$620,000.
- The Virginia Department of Transportation completed improvements to widen Main Street between Kessler Mill Road and Electric Road to four lanes. Of the \$7.5 million total project costs, \$1.1 was the cost of bridge improvements and the remaining was the cost of the street improvements. The project was recognized as a donation of \$1.1 million and \$6.4 million for fiscal year ended 2007 and 2006 respectively.
- Business-type asset activity included two projects. Approximately \$2 million was spent in the current year on the continued construction of two new electric substations and the upgrade of existing electric substations, which will increase the reliability of the City's electric distribution system. The project is expected to be completed in the fall of 2007. Approximately \$1.3 million was spent in the current year on the electric department service center and administrative building, which is expected to be completed in the fall of fiscal year 2009.

LONG-TERM DEBT

At June 30, 2007, the City's long-term liabilities, excluding compensated absences, landfill liability and bond discounts and costs totaled \$96,966,961 comprised of \$32,015,845 related to governmental activities, and \$64,951,116 related to business-type activities. School Division debt of \$19,028,575 is included in the long-term liabilities of governmental activities. Proceeds of \$2.5 million from the 2006 bonds were transferred from business-type to governmental activities to fund on-going capital projects.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Total debt increased by \$2,011,981 during the fiscal year due to an additional \$2,773,019 borrowed from the Virginia Resource Authority to fund upgrades to the regional water pollution control plant. Principal payments made during fiscal year 2007 totaled \$5,060,000. Detailed information regarding these changes in long-term debt is disclosed in Note 7 to the financial statements beginning on page 53.

The City issued \$17,045,000 in general obligation bonds to advance refund \$16,770,000 of outstanding 2002 general obligation bonds. The City completed the advance refunding to take advantage of lower interest rates, reducing future debt service payments of business-type activities.

With its most recent rating, the City maintained a rating of Aa3 from Moody's Investor Service.

The Charter of the City of Salem and the Code of Virginia limits the City's net debt to 10% of the assessed valuation of real estate within the City limits. This limit applies to governmental fund tax supported debt and some long-term liabilities of business-type funds. The City considers long-term debt of its Electric, Water and Sewage Funds to be self-supporting. The City's tax-supported debt of \$32,015,845 is below the legal debt limit of \$163,769,070. Table 10 on page 81 provides additional information.

The School Division relies upon the City to provide full faith and credit for any debt obligations incurred. Therefore, the City reports School Division long-term liabilities, other than compensated absences, as its own. In addition to bonded debt the City's long-term obligations include compensated absences and estimated landfill liability. Additional information concerning the City's long-term liabilities is presented in Note 7 to the financial statements and Table 9 of the statistical section.

Interest and fiscal charges for 2007 were \$1,202,201 or 2.01% of total governmental activities expenses.

FACTORS INFLUENCING FUTURE BUDGETS

Key factors that are expected to impact future budgets include:

- Uncertainty regarding the economy and state funding.
- Projected increases in health insurance premiums and retirement contribution rates assessed by the Virginia Retirement System.
- Funding for the Capital Improvement Program.
- Implementation of the requirements of GASB 45 effective with fiscal year 2008-09.

A rate study for water and sewer is underway and a new rate structure will be instituted in FY08. The new rate structure will benefit customers who conserve, but will result in increases for customers with higher consumption. The City is in the second year of a twenty year contract to purchase electricity. The rate the City pays for wholesale electricity varies based on the supplier's costs.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, tax payers, customers, investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the resources it receives. If you have any questions about this report or need additional information, contact the Director of Finance, City of Salem, 114 North Broad Street, Salem, Virginia 24153, telephone number (540) 375-3061, or visit the City's website at www.ci.salem.va.us

Additional information on the Component Unit can be obtained from the Director of Business Service, Salem Public Schools, 510 South College Avenue, Salem, Virginia 24153.

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BASIC FINANCIAL STATEMENTS

CITY OF SALEM, VIRGINIA
STATEMENT OF NET ASSETS
JUNE 30, 2007

	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	School Division
ASSETS				
Cash and cash equivalents	\$ 4,102,588	\$ 16,063,078	\$ 20,165,666	\$ 5,578,862
Investments	-	3,663,349	3,663,349	-
Receivables, net	2,358,325	4,850,897	7,209,222	1,734
Due from component unit	95,300	-	95,300	-
Due from other governmental units	4,577,232	-	4,577,232	932,499
Internal balances	(8,865)	8,865	-	-
Inventories	442,303	1,550,310	1,992,613	44,963
Prepaid items	-	97,815	97,815	-
<i>Restricted assets:</i>				
Cash and cash equivalents	840,402	14,174,905	15,015,307	-
<i>Capital assets:</i>				
Depreciable, net	94,209,908	66,459,331	160,669,239	39,538,054
Nondepreciable	6,209,102	25,953,111	32,162,213	1,123,637
Total assets	<u>112,826,295</u>	<u>132,821,661</u>	<u>245,647,956</u>	<u>47,219,749</u>
LIABILITIES				
Accounts payable and accrued liabilities	1,791,499	3,848,533	5,640,032	491,661
Accrued interest	248,367	843,077	1,091,444	-
Accrued payroll and related liabilities	829,701	280,371	1,110,072	3,482,039
Self insurance claims liability	132,550	33,111	165,661	-
Due to primary government	-	-	-	95,300
Unearned revenue	86,183	101,591	187,774	14,098
Customer security deposits	-	494,840	494,840	-
<i>Long-term liabilities:</i>				
Due within one year	3,708,272	3,271,502	6,979,774	309,330
Due in more than one year	29,308,460	61,544,858	90,853,318	387,486
Total liabilities	<u>36,105,032</u>	<u>70,417,883</u>	<u>106,522,915</u>	<u>4,779,914</u>
NET ASSETS				
Invested in capital assets, net of related debt	85,853,628	41,636,232	127,489,860	40,661,691
Unrestricted	(9,132,365)	20,767,546	11,635,181	1,778,144
Total net assets	<u>\$ 76,721,263</u>	<u>\$ 62,403,778</u>	<u>\$ 139,125,041</u>	<u>\$ 42,439,835</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2007

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			School Division	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government			Component Unit
					Governmental Activities	Business-type Activities		
Primary government:								
<i>Governmental activities:</i>								
General government administration	\$ 4,803,246	\$ 112,490	\$ 537,585	\$ -	\$ (4,153,171)	\$ (4,153,171)		
Judicial administration	1,540,762	207,525	920,446	-	(412,791)	(412,791)		
Public safety	13,869,676	1,148,627	1,241,695	-	(11,479,354)	(11,479,354)		
Public works	13,476,019	2,892,913	3,312,372	1,168,709	(6,102,025)	(6,102,025)		
Health and welfare	2,193,126	-	782,255	-	(1,410,871)	(1,410,871)		
Education	17,095,000	-	-	-	(17,095,000)	(17,095,000)		
Parks, recreation, and cultural	5,796,220	211,787	229,681	-	(5,354,752)	(5,354,752)		
Community development	1,022,096	3,323	-	-	(1,018,773)	(1,018,773)		
Interest on long-term debt	1,202,201	-	-	-	(1,202,201)	(1,202,201)		
Total governmental activities	60,998,346	4,576,665	7,024,034	1,168,709	(48,228,938)	(48,228,938)		
<i>Business-type activities:</i>								
Electric	24,218,848	29,300,625	-	-	5,081,777	5,081,777		
Water and sewage	11,073,841	10,740,194	-	-	(333,647)	(333,647)		
Civic Center	2,563,090	1,006,344	-	-	(1,556,746)	(1,556,746)		
Catering and concessions	1,103,860	1,097,172	-	-	(6,688)	(6,688)		
Total business-type activities	38,959,639	42,144,335	-	-	3,184,696	3,184,696		
Total primary government	\$ 99,957,985	\$ 46,721,000	\$ 7,024,034	\$ 1,168,709	\$ (48,228,938)	\$ (45,044,242)		
Component unit:								
School division	\$ 40,556,186	\$ 1,570,518	\$ 6,560,448	\$ -		\$ (32,425,220)		
General revenues:								
Property taxes					27,606,560	-		
Meals tax					2,397,412	-		
Local sales and use taxes					5,711,940	-		
Utility taxes					1,228,975	-		
Business license tax					4,258,059	-		
Other taxes					2,700,657	-		
Intergovernmental revenue not restricted					3,878,955	-		
Payments from City of Salem					-	-	17,095,000	
State aid - unrestricted					789,526	928,710	14,317,578	
Unrestricted investment earnings					-	6,967	-	
Gain on sale of property					279,223	20,149	449,800	
Other					495,995	(495,995)	-	
Transfers					49,347,302	459,831	-	
Total general revenues and transfers					1,118,364	3,644,527	31,862,378	
Change in net assets					75,602,899	58,759,251	(562,842)	
Net assets at July 1, restated (Note 15)					\$ 76,721,263	\$ 62,403,778	43,002,677	
Net assets at June 30							\$ 42,439,835	

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2007**

	General	Debt Service	Capital Projects	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 4,102,588	\$ -	\$ -	\$ 4,102,588
Cash and cash equivalents, restricted	-	-	840,402	840,402
Receivables, net	2,348,060	-	10,265	2,358,325
Due from component unit	95,300	-	-	95,300
Due from other governmental units	4,496,960	-	80,272	4,577,232
Inventories	442,303	-	-	442,303
Total assets	<u>\$ 11,485,211</u>	<u>\$ -</u>	<u>\$ 930,939</u>	<u>\$ 12,416,150</u>
LIABILITIES				
Accounts payable and accrued liabilities	\$ 1,820,918	\$ -	\$ 36,153	\$ 1,857,071
Accrued payroll and related liabilities	829,701	-	-	829,701
Self insurance claims liability	132,550	-	-	132,550
Due to other funds	8,865	-	-	8,865
Deferred revenue	788,703	-	-	788,703
Total liabilities	<u>3,580,737</u>	<u>-</u>	<u>36,153</u>	<u>3,616,890</u>
FUND BALANCES				
<i>Reserved for:</i>				
Inventories	442,303	-	-	442,303
Encumbrances	914,731	-	1,083,915	1,998,646
<i>Unreserved, reported in:</i>				
General fund, designated for uninsured claims	610,454	-	-	610,454
Capital projects, undesignated	-	-	(189,129)	(189,129)
General fund, undesignated	5,936,986	-	-	5,936,986
Total fund balances	<u>7,904,474</u>	<u>-</u>	<u>894,786</u>	<u>8,799,260</u>
Total liabilities and fund balances	<u>\$ 11,485,211</u>	<u>\$ -</u>	<u>\$ 930,939</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 governmental funds.	100,419,010
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the governmental funds.	702,520
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds:	
Bonds payable	(32,015,845)
Bond discounts	16,016
Bond costs	561,209
Accrued interest	(248,367)
Compensated absences	(1,512,540)
Net assets of governmental activities	<u>\$ 76,721,263</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
YEAR ENDED JUNE 30, 2007

	General	Debt Service	Capital Projects	Total Governmental Funds
REVENUES				
General property taxes	\$ 27,687,919	\$ -	\$ -	\$ 27,687,919
Other local taxes	16,867,472	-	-	16,867,472
Permits, privilege fees, and regulatory licenses	293,004	-	-	293,004
Fines and forfeitures	159,363	-	-	159,363
Revenue from use of money and property	1,434,893	-	-	1,434,893
Charges for services	3,915,569	-	-	3,915,569
Other	47,673	-	-	47,673
Intergovernmental	10,024,271	273,835	38,764	10,336,870
Total revenues	<u>60,430,164</u>	<u>273,835</u>	<u>38,764</u>	<u>60,742,763</u>
EXPENDITURES				
<i>Current:</i>				
General government administration	4,694,442	-	-	4,694,442
Judicial administration	1,506,395	-	-	1,506,395
Public safety	13,358,739	-	-	13,358,739
Public works	11,434,040	-	-	11,434,040
Health and welfare	2,163,687	-	-	2,163,687
Education	17,095,000	-	-	17,095,000
Parks, recreation, and cultural	4,354,144	-	-	4,354,144
Community development	639,535	-	-	639,535
Non-departmental	1,769,127	-	-	1,769,127
Capital projects	-	-	2,750,335	2,750,335
<i>Debt service:</i>				
Principal retirement	-	2,607,365	-	2,607,365
Interest and fiscal charges	-	1,119,793	-	1,119,793
Total expenditures	<u>57,015,109</u>	<u>3,727,158</u>	<u>2,750,335</u>	<u>63,492,602</u>
Excess (deficiency) of revenues over expenditures	<u>3,415,055</u>	<u>(3,453,323)</u>	<u>(2,711,571)</u>	<u>(2,749,839)</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	1,265,000	3,453,323	2,818,000	7,536,323
Transfers out	(4,627,341)	-	-	(4,627,341)
Total other financing sources (uses)	<u>(3,362,341)</u>	<u>3,453,323</u>	<u>2,818,000</u>	<u>2,908,982</u>
Net change in fund balances	52,714	-	106,429	159,143
FUND BALANCES AT JULY 1	<u>7,851,760</u>	<u>-</u>	<u>788,357</u>	
FUND BALANCES AT JUNE 30	<u>\$ 7,904,474</u>	<u>\$ -</u>	<u>\$ 894,786</u>	

Adjustments for the Statement of Activities:

Governmental funds report capital outlays as expenditures while governmental activities report depreciation expense to allocate the cost of those assets over the life of the assets.	3,956,872
Capital outlay	3,956,872
Donation	1,168,709
Depreciation expense	(3,876,038)
Transfer from proprietary fund	87,013
Governmental funds report proceeds from the sale of a capital asset as an increase in financial resources while governmental activities report the gain or loss on the sale of capital asset.	(362,588)
Proceeds from sale of assets	(362,588)
Gain (loss) from sale of assets	(90,961)
Revenues in the Statement of Activities that do not provide current financial resources are not reported as fund revenues.	150,197
Repayment of bond principal is an expenditure in the governmental funds, but repayment reduces long-term liabilities in the statement of net assets.	(3,558)
Amortization of current year bond discounts	(3,558)
Amortization of current year bond costs	(90,121)
Principal payments	2,607,365
Proceeds transferred in	(2,500,000)
Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	16,948
Change in accrued interest payable	16,948
Change in compensated absences	(104,617)
Change in net assets of governmental activities	<u>\$ 1,118,364</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND
YEAR ENDED JUNE 30, 2007

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		Positive (Negative)
REVENUES				
General property taxes	\$ 30,940,977	\$ 28,137,770	\$ 27,687,919	\$ (449,851)
Other local taxes	17,247,426	17,047,426	16,867,472	(179,954)
Permits, privilege fees, and regulatory licenses	300,500	300,500	293,004	(7,496)
Fines and forfeitures	170,000	145,000	159,363	14,363
Revenue from use of money and property	652,000	712,000	1,434,893	722,893
Charges for services	3,067,550	3,942,550	3,915,569	(26,981)
Other	24,000	24,000	47,673	23,673
Intergovernmental	5,265,221	10,500,372	10,024,271	(476,101)
Total revenues	<u>57,667,674</u>	<u>60,809,618</u>	<u>60,430,164</u>	<u>(379,454)</u>
EXPENDITURES				
<i>Current:</i>				
General government administration	5,405,281	4,831,290	4,694,442	136,848
Judicial administration	1,467,664	1,540,292	1,506,395	33,897
Public safety	12,409,151	13,435,461	13,358,739	76,722
Public works	9,545,228	12,217,815	11,434,040	783,775
Health and welfare	1,070,493	3,017,087	2,163,687	853,400
Education	17,097,500	17,095,000	17,095,000	-
Parks, recreation, and cultural	4,227,627	4,385,208	4,354,144	31,064
Community development	363,908	640,908	639,535	1,373
Non-departmental	3,118,480	2,461,561	1,769,127	692,434
Total expenditures	<u>54,705,332</u>	<u>59,624,622</u>	<u>57,015,109</u>	<u>2,609,513</u>
Excess of revenues over expenditures	<u>2,962,342</u>	<u>1,184,996</u>	<u>3,415,055</u>	<u>2,230,059</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	1,265,000	1,265,000	1,265,000	-
Transfers out	(4,627,342)	(4,627,341)	(4,627,341)	-
Total other financing sources (uses)	<u>(3,362,342)</u>	<u>(3,362,341)</u>	<u>(3,362,341)</u>	<u>-</u>
Net change in fund balances	<u>\$ (400,000)</u>	<u>\$ (2,177,345)</u>	<u>\$ 52,714</u>	<u>\$ 2,230,059</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2007

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
ASSETS				
<i>Current assets:</i>				
Cash and cash equivalents	\$ 14,799,564	\$ 924,207	\$ 339,307	\$ 16,063,078
Investments	3,663,349	-	-	3,663,349
Receivables, net	3,353,046	1,271,347	226,504	4,850,897
Due from other funds	-	8,865	-	8,865
Inventories	1,306,237	224,171	19,902	1,550,310
Prepaid items	-	-	97,815	97,815
Total current assets	<u>23,122,196</u>	<u>2,428,590</u>	<u>683,528</u>	<u>26,234,314</u>
<i>Noncurrent assets:</i>				
Restricted cash	14,174,905	-	-	14,174,905
Capital assets, net	22,318,687	66,894,547	3,199,208	92,412,442
Total noncurrent assets	<u>36,493,592</u>	<u>66,894,547</u>	<u>3,199,208</u>	<u>106,587,347</u>
Total assets	<u>59,615,788</u>	<u>69,323,137</u>	<u>3,882,736</u>	<u>132,821,661</u>
LIABILITIES				
<i>Current liabilities:</i>				
Accounts payable and accrued liabilities	3,015,616	627,251	205,666	3,848,533
Accrued interest	178,922	664,155	-	843,077
Accrued payroll and related liabilities	77,167	95,320	107,884	280,371
Self insurance claims liability	8,575	17,451	7,085	33,111
Unearned revenue	-	-	101,591	101,591
Customer security deposits	494,840	-	-	494,840
Bonds payable	533,887	2,386,808	-	2,920,695
Compensated absences	143,886	144,244	62,677	350,807
Total current liabilities	<u>4,452,893</u>	<u>3,935,229</u>	<u>484,903</u>	<u>8,873,025</u>
<i>Noncurrent liabilities:</i>				
Bonds payable	21,240,779	40,139,878	-	61,380,657
Compensated absences	98,644	40,764	24,793	164,201
Total noncurrent liabilities	<u>21,339,423</u>	<u>40,180,642</u>	<u>24,793</u>	<u>61,544,858</u>
Total liabilities	<u>25,792,316</u>	<u>44,115,871</u>	<u>509,696</u>	<u>70,417,883</u>
NET ASSETS				
Invested in capital assets, net of related debt	14,653,592	23,783,432	3,199,208	41,636,232
Unrestricted	19,169,880	1,423,834	173,832	20,767,546
Total net assets	<u>\$ 33,823,472</u>	<u>\$ 25,207,266</u>	<u>\$ 3,373,040</u>	<u>\$ 62,403,778</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2007

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
OPERATING REVENUES				
Charges for services	\$ 28,626,337	\$ 10,266,647	\$ 2,037,729	\$ 40,930,713
Connections and transfers	14,018	159,228	-	173,246
Penalties	88,313	177,333	-	265,646
Pole rentals	119,450	-	-	119,450
Commissions	-	-	30,952	30,952
Equipment rental credits	264,573	131,881	-	396,454
Other	187,934	5,105	34,835	227,874
Total operating revenues	<u>29,300,625</u>	<u>10,740,194</u>	<u>2,103,516</u>	<u>42,144,335</u>
OPERATING EXPENSES				
Salaries	-	1,815,897	1,449,374	3,265,271
Fringe benefits	-	638,689	422,208	1,060,897
Labor charged to capital improvements	-	(312,696)	-	(312,696)
Show expenses	-	-	171,921	171,921
Maintenance	-	817,182	339,483	1,156,665
Billing and collection	361,434	521,089	-	882,523
Professional services	36,712	35,038	37,238	108,988
Insurance	53,324	81,098	14,971	149,393
Purchased power	18,920,211	-	-	18,920,211
Distribution - operations	1,201,066	-	-	1,201,066
Distribution - maintenance	1,309,503	-	-	1,309,503
Administration	606,049	193,524	26,118	825,691
Travel and training	-	12,462	17,003	29,465
Materials and supplies	-	346,691	380,630	727,321
Utilities	-	265,267	257,507	522,774
Miscellaneous	122,989	8,859	3,124	134,972
Depreciation	846,264	2,541,097	299,770	3,687,131
Amortization	-	55,219	-	55,219
Treatment of sewage	-	2,336,831	-	2,336,831
Commissions	-	-	247,603	247,603
Total operating expenses	<u>23,457,552</u>	<u>9,356,247</u>	<u>3,666,950</u>	<u>36,480,749</u>
Operating income (loss)	<u>5,843,073</u>	<u>1,383,947</u>	<u>(1,563,434)</u>	<u>5,663,586</u>
NONOPERATING REVENUES (EXPENSES)				
Interest income	928,155	-	555	928,710
Interest expense	(761,296)	(1,717,594)	-	(2,478,890)
Decrease in fair value of investments	(142)	-	-	(142)
Gain (loss) on sale of capital assets	9,194	243	(2,470)	6,967
Net nonoperating revenue (expenses)	<u>175,911</u>	<u>(1,717,351)</u>	<u>(1,915)</u>	<u>(1,543,355)</u>
Income (loss) before transfers	<u>6,018,984</u>	<u>(333,404)</u>	<u>(1,565,349)</u>	<u>4,120,231</u>
CAPITAL CONTRIBUTIONS IN TRANSFERS IN	-	20,291	-	20,291
TRANSFERS OUT	-	2,573,594	1,310,583	3,884,177
Change in net assets	<u>(4,284,616)</u>	<u>-</u>	<u>(95,556)</u>	<u>(4,380,172)</u>
Change in net assets	<u>1,734,368</u>	<u>2,260,481</u>	<u>(350,322)</u>	<u>3,644,527</u>
NET ASSETS AT JULY 1	<u>32,089,104</u>	<u>22,946,785</u>	<u>3,723,362</u>	<u>58,759,251</u>
NET ASSETS AT JUNE 30	<u>\$ 33,823,472</u>	<u>\$ 25,207,266</u>	<u>\$ 3,373,040</u>	<u>\$ 62,403,778</u>

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2007**

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
OPERATING ACTIVITIES				
Receipts from customers	\$ 29,326,817	\$ 10,608,782	\$ 1,974,709	\$ 41,910,308
Payments to suppliers	(20,853,515)	(5,613,089)	(1,582,569)	(28,049,173)
Payments to employees	(1,529,224)	(2,171,191)	(1,859,902)	(5,560,317)
Other receipts	187,934	5,105	65,787	258,826
Net cash provided by (used in) operating activities	<u>7,132,012</u>	<u>2,829,607</u>	<u>(1,401,975)</u>	<u>8,559,644</u>
NONCAPITAL FINANCING ACTIVITIES				
Interfund transfers	(1,972,498)	(2,237,502)	1,301,018	(2,908,982)
Net cash provided by (used in) noncapital financing activities	<u>(1,972,498)</u>	<u>(2,237,502)</u>	<u>1,301,018</u>	<u>(2,908,982)</u>
CAPITAL AND RELATED FINANCING ACTIVITIES				
Proceeds from sale of capital assets	-	10,365	-	10,365
Purchases of capital assets	(3,284,128)	(2,573,112)	(461,451)	(6,318,691)
Proceeds from capital debt	-	2,773,019	-	2,773,019
Principal paid on capital debt	(660,000)	(1,792,635)	-	(2,452,635)
Interest paid on capital debt	(1,008,270)	(1,909,679)	-	(2,917,949)
Funds received for payment on bond issuance costs	-	104,288	-	104,288
Net cash used in capital and related financing activities	<u>(4,952,398)</u>	<u>(3,387,754)</u>	<u>(461,451)</u>	<u>(8,801,603)</u>
INVESTING ACTIVITIES				
Proceeds from the sale of investments	298,085	-	-	298,085
Interest received	928,155	-	555	928,710
Net cash provided by investing activities	<u>1,226,240</u>	<u>-</u>	<u>555</u>	<u>1,226,795</u>
Net increase (decrease) in cash and cash equivalents	1,433,356	(2,795,649)	(561,853)	(1,924,146)
CASH AND CASH EQUIVALENTS				
Beginning at July 1	27,541,113	3,719,856	901,160	32,162,129
Ending at June 30	<u>\$ 28,974,469</u>	<u>\$ 924,207</u>	<u>\$ 339,307</u>	<u>\$ 30,237,983</u>
SUMMARY OF CASH AND CASH EQUIVALENTS IN THE STATEMENT OF NET ASSETS				
Cash and cash equivalents	\$ 14,799,564	\$ 924,207	\$ 339,307	\$ 16,063,078
Restricted cash	14,174,905	-	-	14,174,905
	<u>\$ 28,974,469</u>	<u>\$ 924,207</u>	<u>\$ 339,307</u>	<u>\$ 30,237,983</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES				
Operating income (loss)	\$ 5,843,073	\$ 1,383,947	\$ (1,563,434)	\$ 5,663,586
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities				
Depreciation and amortization	846,264	2,596,316	299,770	3,742,350
Change in assets and liabilities				
(Increase) decrease in:				
Receivables, net	125,671	(117,442)	(52,928)	(44,699)
Due from other funds	-	(8,865)	26,212	17,347
Inventories	548,368	(11,383)	7,352	544,337
Prepaid items	-	-	(27,942)	(27,942)
(Decrease) increase in:				
Accounts payable and accrued liabilities	(340,643)	(961,533)	(35,539)	(1,337,715)
Accrued payroll and related liabilities	31,348	(29,301)	11,680	13,727
Self insurance claims liability	(10,524)	(22,132)	(9,315)	(41,971)
Due to other funds	-	-	(21,527)	(21,527)
Customer security deposits payable	90,955	-	-	90,955
Unearned revenue	(2,500)	-	(36,304)	(38,804)
Net cash provided by (used in) operating activities	<u>\$ 7,132,012</u>	<u>\$ 2,829,607</u>	<u>\$ (1,401,975)</u>	<u>\$ 8,559,644</u>
NONCASH CAPITAL AND RELATED FINANCING ACTIVITIES				
Capital assets financed with accounts payable	\$ 717,329	\$ 196,804	\$ -	\$ 914,133
Refunding proceeds placed directly with third party escrow agent	\$ -	\$ 17,755,130	\$ -	\$ -
Refunded debt defeased through third party escrow agent	\$ -	\$ (16,770,000)	\$ -	\$ -
NONCASH INVESTING ACTIVITIES				
Unrealized loss on investments	\$ (142)	\$ -	\$ -	\$ (142)

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2007

	<u>Agency Funds</u>
ASSETS	
Cash and cash equivalents	\$ 509,762
Grant receivable	2,491
Due from Commonwealth of Virginia	<u>104,575</u>
Total assets	<u>\$ 616,828</u>
LIABILITIES	
Accounts payable	\$ 73,137
Liability to agency	<u>543,691</u>
Total liabilities	<u>\$ 616,828</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF CHANGES IN FIDUCIARY ASSETS AND LIABILITIES
JUNE 30, 2007

	Agency Funds
ASSETS	
Balance, Beginning of Year	\$ 537,213
Additions	2,644,454
Deletions	2,564,839
Balance, End of Year	\$ 5,746,506
LIABILITIES	
Balance, Beginning of Year	\$ 537,213
Additions	2,644,454
Deletions	2,564,839
Balance, End of Year	\$ 5,746,506

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies

A. The Financial Reporting Entity

The Town of Salem was established by act of the Virginia General Assembly in 1806. The City of Salem, Virginia (City) was established by act of the Virginia General Assembly in 1968. It is a political subdivision of the Commonwealth of Virginia, operating under the Council-manager form of government. The City Council consists of a mayor and four other council members. The City is not part of a county and has taxing powers subject to state-wide restrictions and tax limits. The City of Salem is the primary government of the reporting entity.

The City provides a full range of municipal services including police and fire, sanitation, health and social services, public improvements, planning and zoning, general administrative services, education, electric, water, and sewer services.

The following entities are excluded from the accompanying financial statements:

Joint Ventures

Roanoke Valley Regional Board

The City of Salem School Division, along with Counties of Botetourt, Craig and Franklin and the City of Roanoke jointly participate in a regional education program for severely handicapped students operated by the Roanoke Valley Regional Board (Regional Board). The Regional Board is composed of five members, one from each participating locality. The City has control over budget and financing of the venture only to the extent of representation by the Regional Board member appointed. Each locality's financial obligation is based on their proportionate share of students attending the regional program. For the year ended June 30, 2007, the City's proportionate share was \$389,754, which was paid by the City of Salem School Division. Financial statements can be obtained from the Executive Director of The Roanoke Valley Regional Board at 12 Barron Drive, Suite 1, Troutville, Virginia, 24175.

Roanoke Valley Regional Fire – EMS Training Center

The City, along with the County of Roanoke, the City of Roanoke and the Town of Vinton, jointly operate a fire/EMS training center (Center). The Center is governed by a committee designated by the participating jurisdictions. New fire/EMS recruits are required to take a five-month training course at the facility before being assigned to a station. After completion of the training, the new recruits are state certified. Each jurisdiction is responsible for a percentage of the annual operating costs of the facility. The City of Salem is responsible for 8% of the annual operating costs. For the fiscal year ended June 30, 2007, the City paid \$6,000 of the total annual operating costs of the facility. Financial statements may be obtained from the Roanoke Valley Regional Fire/EMS Training Center, 1220 Kessler Mill Road, Salem, Virginia 24153.

Western Virginia Regional Jail Authority

The City, along with the Counties of Franklin, Montgomery and Roanoke formed the Western Virginia Regional Jail Authority (WVRJA) on May 25, 2005 for the purpose of developing and operating a regional jail for the benefit of Member Jurisdictions. The Board consists of three representatives from each of the Member Jurisdictions. The Member Jurisdictions will each be responsible for a per diem cost based on prisoner days used. The new jail is currently under construction and is expected to be operational by the spring of 2009.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies (Continued)

A. The Financial Reporting Entity (Continued)

Jointly Governed Organizations

Roanoke Valley Detention Commission

The Counties of Botetourt, Craig, and Roanoke and the Cities of Roanoke and Salem formed the Roanoke Valley Detention Commission (Commission) to renovate, expand and operate a detention facility for juveniles. The Commission is governed by a six-member board. Each locality's financial obligation is based on the number of juveniles housed at the facility. The Commission has the authority to issue debt and such debt is the responsibility of the Commission. For the fiscal year ended June 30, 2007, the City remitted \$244,584 in per diem charges.

Blue Ridge Behavioral Healthcare

The Counties of Botetourt, Craig, and Roanoke and the Cities of Roanoke and Salem formed Blue Ridge Behavioral Healthcare (BRBH) to provide a system of comprehensive community mental health, mental retardation and substance abuse services. BRBH is governed by a sixteen-member board. Each locality's financial obligation is based on the type and amount of services performed for individuals in the locality. For the fiscal year ended June 30, 2007, the City remitted \$102,000 to BRBH.

Fifth District Employment and Training Consortium

The Counties of Alleghany, Botetourt, Craig, and Roanoke, the Cities of Covington and Salem and the Town of Clifton Forge jointly participate in the Fifth District Employment and Training Consortium (Consortium). The Consortium is governed by an eight-member board.

Fifth Planning District Disability Services Board

The Counties of Alleghany, Botetourt, Craig, and Roanoke, the Cities of Covington, Roanoke and Salem and the Towns of Clifton Forge and Vinton, jointly participate in the Fifth Planning District Disability Services Board (Services Board). The Services Board provides input to state and local agencies on service needs and priorities of persons with physical and sensory disabilities.

B. Individual Component Unit Disclosure

Discretely Presented Component Unit

The City of Salem School Division (School Division) is a legally separate entity which operates four elementary schools, one middle school, and one high school. School Board members are appointed by City Council. City Council also provides fiscal guidance because it levies taxes for the School Division's operations and issues debt for its capital projects. Based on these facts, the City reports the School Division as a discretely presented component unit. Separately issued financial statements may be obtained by contacting the City of Salem Schools, Director of Business Services, 510 South College Avenue, Salem, Virginia 24153.

C. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007

1. Summary of Significant Accounting Policies (Continued)

C. Government-Wide and Fund Financial Statements (Continued)

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

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

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

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

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* 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 electric and the water and sewage enterprise funds are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies (Continued)

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

Agency funds are unlike all other types of funds, reporting only assets and liabilities; therefore, agency funds do not have a measurement focus.

The City reports the following major governmental funds:

- The *general fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- The *debt service fund* accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.
- The *capital projects fund* accounts for financial resources to be used for the acquisition or construction of major capital facilities.

The City reports the following major proprietary funds:

- The *electric fund* accounts for the activities of the electric distribution operations.
- The *water and sewage fund* accounts for the activities of the water and sewer operations.

Additionally, the City reports the following fund type:

- The *agency funds* are used to account for monies held on behalf of the Cardinal Criminal Justice Academy, and Court-Community Criminal Justice Board in purely a custodial capacity.

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

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the government's proprietary funds and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies (Continued)

E. Budgets and Budgetary Accounting

The City's budget is presented in accordance with accounting principles generally accepted in the United States of America. The following procedures are used by the City in establishing the budgetary data reflected in the financial statements:

- Thirty days prior to the last council meeting in May, the City Manager submits to City Council a proposed operating and capital budget for the fiscal year commencing the following July 1. This budget includes proposed expenditures and the means of financing them for the general fund. The Capital Projects Fund utilizes a project length budget in lieu of an annual budget; therefore, no annual budgets for capital projects are presented.
- Public hearings are conducted to obtain citizen comments.
- Prior to June 30, the budgets are legally enacted through passage of an Appropriations Ordinance. City Council may, from time to time, amend the budget providing for additional expenditures and the means for financing them. City Council approved additional appropriations of \$4,919,290 during the current year primarily for grants, to reappropriate funds for encumbrances and to cover additional operating expenditures.
- The Appropriations Ordinance places legal restrictions on expenditures at the department or function level. The City Manager is authorized to transfer budget amounts within and between the general government departments and categories.
- Formal budgetary integration is employed as a management control device for the general funds.
- All budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America.
- All appropriations lapse on June 30 except for the capital projects fund, which carry unexpended balances into the following year.

F. Encumbrances

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of monies are recorded in order to reserve that portion of the appropriation, is employed as an extension of formal budgetary integration in the general fund. Encumbrances outstanding at year end are reported as reservations of fund balances since they do not constitute expenditures or liabilities. These encumbrances are subject to reappropriation by City Council in the subsequent fiscal year.

G. Cash and Cash Equivalents and Investments

The City considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

Investments are stated at fair value.

H. Allowance for Uncollectible Accounts

The City calculates its allowance for uncollectible accounts using historical collection data and specific account analysis.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies (Continued)

I. Inventory

Governmental fund inventories consist of street and building materials and general supplies held for consumption. Inventories are valued at cost using the first-in, first-out (FIFO) method. Disbursements for inventory are considered to be expenditures at the time of use (consumption method of accounting). Supplies transferred to and consumed by the individual departments are considered a reduction of inventory and an expenditure of the user department.

Enterprise fund inventories consist principally of spare parts held for consumption. Electric fund inventories are valued at cost using the average cost method. All other enterprise fund inventories are valued at cost using the FIFO method. The cost of spare parts is recorded as an expense at the time inventory is withdrawn for use.

J. Prepaid Items

Prepaid items include, among other items, costs incurred as of June 30, which are directly related to Civic Center shows and events scheduled for the subsequent fiscal year. Such costs are expensed in the subsequent fiscal year to obtain a proper matching of revenues and expenses.

K. Capital Assets

Capital assets, which include property, plant and equipment, and infrastructure assets, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial individual cost of more than \$0 for land, \$5,000 for machinery and equipment or \$10,000 for buildings, plant, and infrastructure and an estimated useful life in excess of five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value on the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

Buildings and improvements	10-50 years
Machinery and equipment	5-25 years
Distribution and transmission systems	35 years
Public domain infrastructure	50 years
Utility plant	35 years
Sewage treatment contract	40 years
Furniture and equipment	5-10 years

L. Capitalization of Interest

The City follows the policy of capitalizing net interest costs on funds borrowed to finance the construction of proprietary capital assets. Interest is not capitalized on the construction of assets used in governmental activities. Interest of \$269,772 was capitalized for the year ended June 30.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

1. Summary of Significant Accounting Policies (Continued)

M. School Division Capital Assets and Related Debt Reporting

Local governments in Virginia have a “tenancy in common” with the School Board whenever the locality incurs a financial obligation, excluding capital leases, for school property which is payable over more than one fiscal year. The primary government reports this debt in its financial statements while the Component Unit School Division reports the capital asset.

N. Deferred and Unearned Revenue

Deferred revenue in the general fund consists primarily of property taxes not collected within 60 days of year end and property taxes collected that are not yet due.

Unearned revenue in the nonmajor enterprise funds represents amounts received by the Civic Center as deposits for events or rentals associated with the subsequent year.

O. Compensated Absences

The City and the School Division have policies which allow for the accumulation and vesting of limited amounts of vacation and sick leave until termination or retirement. Amounts of such absences are accrued when incurred in the government-wide, proprietary, and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds when the amounts are due for payment.

P. Long-Term Obligations

In the government-wide financial statements and proprietary funds in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund statement of net assets. Bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Q. Fund Equity

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

R. Estimates

Management uses estimates and assumptions in preparing its financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities, and reported revenues, expenditures, and expenses. Actual results could differ from those estimates.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

2. Deposits and Investments

Deposits

All cash of the City and component unit School Division is maintained in accounts collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400 of the *Code of Virginia* or covered by federal depository insurance.

Investments

Statutes authorize local governments and other public bodies to invest in obligations of the United States or agencies thereof, obligations of the Commonwealth of Virginia or political subdivisions thereof, obligations of the International Bank for Reconstruction and Development (World Bank), the Asian Development Bank, the African Development Bank, prime quality commercial paper and certain corporate notes; banker's acceptances, repurchase agreements, the State Treasurer's Local Government Investment Pool (LGIP), and the State Treasurer's Non-Arbitrage Program (SNAP).

During the year, the City had invested bond proceeds subject to rebate of arbitrage earnings in the SNAP, which is designed to assist local governments in complying with the arbitrage rebate requirements of the Tax Reform Act of 1986. These programs provide comprehensive investment management, accounting and arbitrage rebate calculation services for proceeds of general obligation and revenue tax-exempt financing of Virginia counties, cities and towns.

Credit Risk

State statute requires that obligations of the Commonwealth of Virginia and its political subdivisions have a debt rating of at least AA by Standard & Poor's (S&P) or Aa by Moody's Investors Service (Moody's). Repurchase agreements are collateralized by Treasury or Agency obligations of which the market value is at least 102% of the purchase price of the agreement. Commercial paper must be issued by an entity incorporated in the U.S. and rated at least A-1 by S&P and P-1 by Moody's. Corporate notes and bonds have a rating of at least AA by S&P and Aa by Moody's. Money market mutual funds must trade on a constant net asset value and invest solely in securities otherwise eligible for investment under these guidelines.

As of June 30, 15% of the portfolio was invested in "AAA" rated securities, 1% was invested in "AA1" rated securities, 1% was invested in "AA2" rated securities, 2% was invested in "AA3" rated securities, <1% was invested in "A1" rated securities, <1% was invested in "A2" rated securities, and 78% was invested in "P-1" rated commercial paper. The remaining 2% of the portfolio was invested in money market accounts guaranteed by the U.S. Government. All credit ratings presented in this paragraph are either S&P or Moody's ratings.

Concentration of Credit Risk

Although the intent of the City is to diversify its investment portfolio to avoid incurring unreasonable risks regarding (i) security type, (ii) individual financial institution or issuing entity, and (iii) maturity, the City places no limit on the amount it may invest in any one issuer.

As of June 30, the portions of the portfolio with a single issuer that exceed 5% of the total portfolio are as follows:

<u>Issuer</u>	<u>Percentage of Portfolio</u>
SNAP	78%
Other Federal Obligations	8%
Corporate Obligations	5%

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

2. Deposits and Investments (Continued)

Interest Rate Risk

The City manages its exposure to fair value losses arising from increasing interest rates by limiting the length of each investment to achieve a minimal portfolio average maturity.

As of June 30, the fair values and weighted average maturity of the investments were as follows:

Investment Type	Fair Value	Average Maturity*
Corporate Obligations	\$ 821,755	218
U.S. Treasury Bills	273,574	290
Municipal Obligations	248,916	56
Other Federal Obligations	1,514,449	20
Federal National Mortgage Association	597,188	269
Federal Home Loan Bank	207,467	170
Money Market	290,206	1
SNAP	14,174,905	1
Total Investments	<u>\$ 18,128,460</u>	
Portfolio weighted average maturity		<u>28</u>

* Average maturity in days.

Custodial Credit Risk

As required by the *Code of Virginia*, all security holdings with maturities over 30 days may not be held in safekeeping with the "counterparty" to the investment transaction. As of June 30, all of the City's investments are held in a bank's trust department in the City's name by the City's designated custodian.

All investment activity during the year was in securities of the type held at year end. The previous items are reflected in the statements as follows:

	Primary Government	Component Unit-School Division
Cash and cash equivalents	\$ 20,165,666	\$ 5,578,862
Investments	3,663,349	-
Cash and cash equivalents, restricted	15,015,307	-
	<u>\$ 38,844,322</u>	<u>\$ 5,578,862</u>

Restricted cash and cash equivalents consist of unused bond proceeds and amounts for capital projects.

3. Receivables

Receivables are as follows:

	General	Capital Projects	Electric	Water and Sewage	Nonmajor Enterprise Funds	Component Unit-School Division
Taxes	\$ 1,240,182	\$ -	\$ -	\$ -	\$ -	\$ -
Accounts	-	-	3,476,160	1,331,964	234,897	-
Other	1,526,549	10,265	-	-	-	1,734
Gross receivables	2,766,731	10,265	3,476,160	1,331,964	234,897	1,734
Less allowance for:						
uncollectibles	418,671	-	123,114	60,617	8,393	-
Net total receivables	<u>\$ 2,348,060</u>	<u>\$ 10,265</u>	<u>\$ 3,353,046</u>	<u>\$ 1,271,347</u>	<u>\$ 226,504</u>	<u>\$ 1,734</u>

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

3. Receivables (Continued)

Governmental funds report *deferred revenue* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At June 30, the components of *deferred revenue* reported in the governmental funds were as follows:

	Unavailable	Unearned	Total
Delinquent property taxes receivable	\$ 578,353	\$ -	\$ 578,353
Fees paid in advance	-	176,813	176,813
Taxes paid for subsequent year	-	33,537	33,537
	<u>\$ 578,353</u>	<u>\$ 210,350</u>	<u>\$ 788,703</u>

4. Interfund Receivables, Payables, and Transfers

The composition of the interfund receivables and payables is as follows:

Receivable Fund	Payable Fund	Amount
Water and Sewage Fund	General Fund	\$ 8,865
		<u>\$ 8,865</u>

The amount due from the general fund to the water and sewage fund represents receipts from sale of capital assets that have not yet been transferred.

The composition of the interfund transfers are as follows:

	Transfers In:					Total
	General	Debt Service	Capital Project	Water and Sewage	Nonmajor Enterprise	
Transfers out:						
General	\$ -	\$3,453,323	\$ -	\$ -	\$ 1,174,018	\$ 4,627,341
Electric	1,265,000	-	2,818,000	2,573,594	127,000	6,783,594
Nonmajor Enterprise	-	-	-	-	9,565	9,565
	<u>\$1,265,000</u>	<u>\$3,453,323</u>	<u>\$2,818,000</u>	<u>\$2,573,594</u>	<u>\$ 1,310,583</u>	<u>\$11,420,500</u>

Transfers between major funds and other nonmajor enterprise funds were primarily for debt payments, operation of funds, and reimbursement of capital items paid by the general fund. \$2,500,000 of the original 2006A public improvement general obligation bond was moved from the electric fund to the capital projects fund to finance several projects. This amount is shown in the financials as a transfer in for the capital project fund, however it is not shown as a transfer in the electric fund. The electric and civic center funds transferred capital assets totaling \$1,022 and \$85,991 respectively, to the general fund resulting in a \$87,013 reconciling item for interfund transfers for the governmental funds between Exhibit 2 and Exhibit 4.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

5. Due from Other Governmental Units

Amounts due from other governmental units are as follows:

	Governmental Activities	Component Unit-School Division
Commonwealth of Virginia		
Personal property tax	\$ 2,588,707	\$ -
State sales tax	-	533,489
Local sales tax	1,014,314	-
Communications tax	88,020	-
Constitutional officers	112,649	-
Comprehensive services act	561,207	-
Other	212,335	-
Federal government		
School funds	-	399,010
	<u>\$ 4,577,232</u>	<u>\$ 932,499</u>

6. Capital Assets

Capital asset activity for the year was as follows:

Governmental Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not depreciated				
Land	\$ 4,502,611	\$ 393,776	\$ 70,270	\$ 4,826,117
Construction in progress	16,488,332	1,082,283	16,187,630	1,382,985
Total capital assets, not depreciated	<u>20,990,943</u>	<u>1,476,059</u>	<u>16,257,900</u>	<u>6,209,102</u>
Capital assets, depreciated				
Buildings and improvements	28,204,130	9,830,846	415,380	37,619,596
Machinery and equipment	14,139,915	2,135,133	764,095	15,510,953
Public domain infrastructure	77,767,348	8,474,772	27,015	86,215,105
Total capital assets, depreciated	<u>120,111,393</u>	<u>20,440,751</u>	<u>1,206,490</u>	<u>139,345,654</u>
Less accumulated depreciation				
Buildings and improvements	8,806,146	937,843	126,856	9,617,133
Machinery and equipment	9,585,208	1,331,814	681,789	10,235,233
Public domain infrastructure	23,174,979	2,117,194	8,793	25,283,380
Total accumulated depreciation	<u>41,566,333</u>	<u>4,386,851</u>	<u>817,438</u>	<u>45,135,746</u>
Total capital assets, depreciated net	<u>78,545,060</u>	<u>16,053,900</u>	<u>389,052</u>	<u>94,209,908</u>
Governmental activities capital assets, net	<u>\$ 99,536,003</u>	<u>\$ 17,529,959</u>	<u>\$ 16,646,952</u>	<u>\$ 100,419,010</u>

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

6. Capital Assets (Continued)

Business-Type Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not depreciated				
Land	\$ 1,252,171	\$ -	\$ -	\$ 1,252,171
Construction in progress	18,244,191	6,558,703	101,954	24,700,940
Total capital assets, not depreciated	<u>19,496,362</u>	<u>6,558,703</u>	<u>101,954</u>	<u>25,953,111</u>
Capital assets, depreciated				
Buildings and improvements	7,587,549	273,591	329,815	7,531,325
Distribution and transmission	20,590,518	202,444	10,328	20,782,634
Utility plant	70,918,118	128,266	42,722	71,003,662
Sewage treatment contract	18,297,088	-	-	18,297,088
Machinery and equipment	5,866,553	731,030	741,052	5,856,531
Total capital assets, depreciated	<u>123,259,826</u>	<u>1,335,331</u>	<u>1,123,917</u>	<u>123,471,240</u>
Less accumulated depreciation				
Buildings and improvements	3,642,015	264,674	235,131	3,671,558
Distribution and transmission	13,585,973	571,067	7,022	14,150,018
Utility plant	31,395,767	1,929,294	102	33,324,959
Sewage treatment contract	1,829,658	457,427	-	2,287,085
Machinery and equipment	3,636,778	602,596	661,085	3,578,289
Total accumulated depreciation	<u>54,090,191</u>	<u>3,825,058</u>	<u>903,340</u>	<u>57,011,909</u>
Total capital assets, depreciated net	<u>69,169,635</u>	<u>(2,489,727)</u>	<u>220,577</u>	<u>66,459,331</u>
Business-type activities capital assets, net	<u>\$ 88,665,997</u>	<u>\$ 4,068,976</u>	<u>\$ 322,531</u>	<u>\$ 92,412,442</u>

Included in the construction in progress increase is \$585,742 of transformer costs, which were recorded in inventory in prior years. The classification was changed to better align the idle transformers with the distribution system.

Component Unit - School Division	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not depreciated				
Land	\$ 1,123,637	\$ -	\$ -	\$ 1,123,637
Construction in progress	231,023	-	231,023	-
Total capital assets, not depreciated	<u>1,354,660</u>	<u>-</u>	<u>231,023</u>	<u>1,123,637</u>
Capital assets, depreciated				
Buildings and improvements	51,191,156	624,992	105,294	51,710,854
Furniture and equipment	5,052,820	115,526	168,092	5,000,254
Total capital assets, depreciated	<u>56,243,976</u>	<u>740,518</u>	<u>273,386</u>	<u>56,711,108</u>
Less accumulated depreciation				
Buildings and improvements	13,289,144	1,267,315	54,808	14,501,651
Furniture and equipment	2,500,490	326,833	155,920	2,671,403
Total accumulated depreciation	<u>15,789,634</u>	<u>1,594,148</u>	<u>210,728</u>	<u>17,173,054</u>
Total capital assets, depreciated net	<u>40,454,342</u>	<u>(853,630)</u>	<u>62,658</u>	<u>39,538,054</u>
Component unit capital assets, net	<u>\$ 41,809,002</u>	<u>\$ (853,630)</u>	<u>\$ 293,681</u>	<u>\$ 40,661,691</u>

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

6. Capital Assets (Continued)

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities	
General government administration	\$ 219,822
Judicial administration	36,935
Public safety	583,500
Public works	2,388,883
Parks, recreation, and cultural	639,691
Community development	7,207
Total depreciation expense	<u>\$ 3,876,038</u>
Business-type activities	
Electric	\$ 846,264
Water and sewage	2,541,097
Civic Center	286,171
Catering	13,599
Total depreciation expense	<u>\$ 3,687,131</u>

Construction Commitments

The City has an active construction project at June 30 as follows:

<u>Project</u>	<u>Spent to Date</u>	<u>Remaining Contract</u>
Salem High School exterior parapet wall	<u>\$ 32,828</u>	<u>\$ 52,154</u>

Sewage Treatment Contract

The sewage treatment contract represents a 1994 agreement between the Cities of Salem and Roanoke along with the Counties of Roanoke and Botetourt and the Town of Vinton to provide for the transportation and treatment of waste for a 40-year period. On July 1, 2004, the Western Virginia Water Authority (WVWA) was created by the City of Roanoke and the County of Roanoke. The WVWA is a full service authority that provides water and wastewater treatment to the Roanoke Valley region. This authority assumed the contractual obligation to provide wastewater treatment to the City of Salem. Rates are adjusted annually.

7. Long-Term Liabilities

The government issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. General obligation bonds have been issued for both governmental and business-type activities. These bonds are direct obligations and pledge the full faith and credit of the government. In addition, the government issues bonds where the government pledges income derived from the acquired or constructed assets to pay debt service (revenue bonds). Revenue bonds have been issued for the business-type activities only.

Prior Year Defeasances of Debt

In prior years, the City defeased certain general obligation bonds by placing the proceeds in irrevocable trusts to provide for all future debt service on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City's financial statements. On June 30, 2007, \$11,375,000 of bonds were considered defeased. The deferred costs are being amortized over the life of the new bonds as a component of interest expense.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

7. Long-Term Liabilities (Continued)

Current Year Defeasances of Debt

On March 15, 2007, the City issued \$17,045,000 in general obligation bonds with an average interest rate of 4.7% to advance refund \$16,770,000 of outstanding 2002 general obligation bonds with an average interest rate of 5.2%. The net proceeds of approximately \$17,755,130 (after payment of \$100,000 in issuance costs, \$85,225 in underwriter's compensation and \$2,458 in additional proceeds) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for future debt service payments on the 2002 general obligation bonds. As a result, \$16,770,000 of the 2002 general obligation bonds are considered to be defeased and the liability for those bonds has been removed from the financial statements.

The advance refunding resulted in a difference between the reacquisition price and the net carrying value of the old debt of \$1,010,778. This difference, reported in the accompanying financial statements as a subtraction from bonds payable, is being amortized over the life of the new bond as a component of interest expense through the year 2027. The City completed the advance refunding to reduce its total debt service payments by \$732,647 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$792,348.

Details of long-term indebtedness are as follows:

	<u>Interest Rates</u>	<u>Date Issued</u>	<u>Final Maturity Date</u>	<u>Amount of Original Issue</u>	<u>Governmental Activities</u>	<u>Business- type Activities</u>
<u>General Obligation Bonds</u>						
1999 Public Improvement	4.0-4.9%	04-99	04-19	\$17,000,000	\$ 3,000,000	\$ 7,200,000
2002 Public Improvement	4.5-5.0%	01-02	01-12	23,000,000	-	3,455,000
2003A Public Improvement	2.0-4.5%	10-03	10-23	22,000,000	18,700,000	-
2003B Refunding	2.0-3.5%	10-03	12-12	5,700,000	3,650,000	-
2004 Refunding	1.5-3.5%	03-04	04-16	9,640,000	3,665,845	4,609,155
2006A Public Improvement	4.0-5.0%	05-06	04-31	25,000,000	2,500,000	21,840,000
2007A Refunding	4.0-5.0%	02-07	01-27	17,045,000	-	17,045,000
					<u>31,515,845</u>	<u>54,149,155</u>
			Add bond premium		-	991,942
			Less bond discounts		(16,016)	-
			Less deferred costs		(561,209)	(1,641,706)
					<u>\$30,938,620</u>	<u>\$53,499,391</u>
<u>Other Long-term Debt</u>						
Literary Fund Loan	4.0%	01-91	02-11	2,500,000	<u>\$ 500,000</u>	<u>\$ -</u>
<u>Revenue Bonds</u>						
Virginia Resource Authority	3.0%	04-04	Varies	10,801,961 *	<u>\$ -</u>	<u>\$10,801,961</u>

* Amount represents drawdowns at June 30 on total approved loan of \$11,052,222.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007

7. Long-Term Liabilities (Continued)

The annual requirements to amortize long-term debt and related interest are as follows:

Governmental Activities Year Ended June 30,	General Obligation Bonds		Literary Fund Loans	
	Principal	Interest	Principal	Interest
2008	\$ 2,487,403	\$ 1,151,197	\$ 125,000	\$ 20,000
2009	2,493,896	1,090,217	125,000	15,000
2010	2,468,118	1,019,642	125,000	10,000
2011	2,442,415	941,216	125,000	5,000
2012	2,421,617	859,860	-	-
2013-2017	9,249,623	3,089,762	-	-
2018-2022	6,509,963	1,475,738	-	-
2023-2027	2,828,081	327,037	-	-
2028-2032	614,729	71,526	-	-
	<u>\$ 31,515,845</u>	<u>\$ 10,026,195</u>	<u>\$ 500,000</u>	<u>\$ 50,000</u>

Business-type Activities Year Ended June 30,	General Obligation Bonds		Revenue Bonds	
	Principal	Interest	Principal	Interest
2008	\$ 2,522,597	\$ 2,213,662	\$ 398,098	\$ 324,059
2009	2,401,104	2,284,559	410,041	312,116
2010	2,446,882	2,194,071	422,342	299,815
2011	2,487,585	2,100,547	435,012	287,144
2012	2,538,383	2,003,022	448,062	274,094
2013-2017	12,905,377	8,368,357	2,450,189	1,160,593
2018-2022	11,140,037	5,565,518	2,840,440	770,342
2023-2027	12,336,919	2,944,335	3,292,849	317,933
2028-2032	5,370,271	624,851	104,928	3,148
	<u>\$ 54,149,155</u>	<u>\$ 28,298,922</u>	<u>\$ 10,801,961</u>	<u>\$ 3,749,244</u>

The following is a summary of changes in long-term liabilities:

	Beginning Balance	Additions	Reductions	Transfers	Ending Balance	Due Within One Year
Governmental Activities						
General obligation bonds	\$ 31,498,210	\$ -	\$ 2,482,365	\$ 2,500,000	\$ 31,515,845	\$ 2,487,403
Literary fund loans	625,000	-	125,000	-	500,000	125,000
Landfill closure liability	57,189	8,383	-	-	65,572	65,572
Compensated absences	1,407,923	2,078,888	1,974,271	-	1,512,540	1,030,297
<i>Adjust for deferred amounts:</i>						
Issuance discounts	(19,574)	-	(3,558)	-	(16,016)	-
Issuance costs	(651,330)	-	(90,121)	-	(561,209)	-
Governmental activities, long-term liabilities	<u>\$ 32,917,418</u>	<u>\$ 2,087,271</u>	<u>\$ 4,487,957</u>	<u>\$ 2,500,000</u>	<u>\$ 33,016,732</u>	<u>\$ 3,708,272</u>
Business-type Activities						
General obligation bonds	\$ 58,826,790	\$ 17,045,000	\$ 19,222,635	\$ (2,500,000)	\$ 54,149,155	\$ 2,522,597
Revenue Bonds	8,028,942	2,773,019	-	-	10,801,961	398,098
Compensated absences	519,752	498,270	503,014	-	515,008	350,807
<i>Adjust for deferred amounts:</i>						
Issuance premiums	136,908	897,814	42,780	-	991,942	-
Issuance costs	(604,673)	(1,149,392)	(112,359)	-	(1,641,706)	-
Business-type activities, long-term liabilities	<u>\$ 66,907,719</u>	<u>\$ 20,064,711</u>	<u>\$ 19,656,070</u>	<u>\$ (2,500,000)</u>	<u>\$ 64,816,360</u>	<u>\$ 3,271,502</u>
Component Unit - School Division						
Compensated absences	<u>\$ 576,835</u>	<u>\$ 211,701</u>	<u>\$ 91,720</u>	<u>\$ -</u>	<u>\$ 696,816</u>	<u>\$ 309,330</u>

The general fund has been used to liquidate the liability for compensated absences in prior years.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

8. Landfill Closure and Post-closure Care Costs

The City stopped accepting waste at its municipal landfill prior to October 9, 1993. State and federal regulations required the City to place a final cover on the landfill site and to perform certain maintenance and monitoring functions at the site for ten years after closure. Post-closure maintenance and monitoring costs are currently estimated at \$25,000 annually and commenced during 1998. Actual cost may be higher due to inflation, changes in technology, or changes in regulations. These costs are being recognized as expenditures under the modified accrual basis of accounting. The cumulative accrual is reported with the governmental activities long-term liabilities. The City uses the financial test method of demonstrating assurance for closure and post-closure care cost.

9. Pension Plan

Plan Description

The City contributes to the Virginia Retirement System (VRS), an agent and cost sharing multiple-employer defined benefit pension plan administered by the Virginia Retirement System (System). In addition, professional and non-professional employees of the City of Salem School Division are covered by the VRS. Professional employees participate in a VRS statewide teacher cost sharing pool, and non-professional employees participate as a separate group in the agent multiple-employer retirement system.

All full-time, salaried permanent employees of participating employers must participate in the VRS. Benefits vest after five years of service. Employees are eligible for an unreduced retirement benefit at age 65 with 5 years of service (age 60 with 5 years of service for participating law enforcement officers and firefighters) or at age 50 with 30 years of service for participating employers (age 50 with 25 years of service for participating law enforcement officers and firefighters) payable monthly for life in an amount equal to 1.7% of their average final compensation (AFC) for each year of credited service. Benefits are actuarially reduced for retirees who retire prior to becoming eligible for full retirement benefits. In addition, retirees qualify for an annual cost-of-living adjustment (COLA) beginning in their second year of retirement. The COLA is limited to 5% per year. AFC is defined as the highest consecutive 36 months of reported compensation. Participating law enforcement officers and firefighters may receive a monthly benefit supplement if they retire prior to age 65. The VRS also provides death and disability benefits. Title 51.1 of the *Code of Virginia* (1950), as amended, assigns the authority to establish and amend benefit provisions to the General Assembly of Virginia.

The System issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information for VRS. A copy of that report may be downloaded from <http://www.varetire.org/Pdf/Publications/2006annurept.pdf> or obtained by writing to the System at P.O. Box 2500, Richmond, Virginia 23218-2500.

Funding Policy

Plan members are required by Title 51.1 of the *Code of Virginia* (1950), as amended, to contribute 5% of their annual reported compensation to the VRS. This 5% member contribution has been assumed by both the City and School Division. In addition, the City and School Division are required to contribute the remaining amounts necessary to fund its participation in the VRS using the actuarial basis specified by the statute and approved by the VRS Board of Trustees. The City's and the School Division's non-professional contribution rates for the fiscal year ended June 30 were 15.52% and 10.11% of the annual covered payroll, respectively (including the employee share of 5% paid by the employer).

For the three years ended June 30, 2007, 2006, and 2005, total employer and employee contributions made to the VRS statewide teacher pool for professional employees by the School Division were \$2,921,443, \$2,314,322, and \$2,061,238, representing 14.20%, 11.62%, and 11.03%, of annual covered payroll, respectively.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

9. Pension Plan (Continued)

Annual Pension Cost

For fiscal year June 30 the City's and the School Division's annual pension cost of \$5,397,504 and \$143,720, respectively, were equal to their required and actual contributions. The required contribution was determined as part of the June 30, 2006 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included (a) 7.5% investment rate of return, (b) projected salary increases ranging from 3.75% to 5.60% per year, and (c) 2.5% per year cost-of-living adjustments. Both (a) and (b) included an inflation component of 2.5%. The actuarial value of the City's and the School Division's assets is equal to the modified market value of assets. This method was determined using techniques that smooth the effects of short-term volatility in the market value of assets over a five-year period. The City's and School Division's actuarial accrued liabilities are being amortized as a level percentage of payroll on an open basis within a period of 20 years or less.

Three-Year Trend Information for the City

<u>Fiscal Year Ending</u>	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
June 30, 2007	\$ 5,397,504	100%	\$ -
June 30, 2006	\$ 4,949,519	100%	\$ -
June 30, 2005	\$ 4,704,758	100%	\$ -

**Three-Year Trend Information for the School Division
Non-Professional Staff**

<u>Fiscal Year Ending</u>	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
June 30, 2007	\$ 143,720	100%	\$ -
June 30, 2006	\$ 109,561	100%	\$ -
June 30, 2005	\$ 103,329	100%	\$ -

10. Other Post-Employment Benefits

The City provides healthcare benefits under current personnel policy to retired employees under one of two programs. In the first, retirees 65 and under who are ineligible for the Nationwide Medicare Program are allowed to continue in the City's health insurance program described in Note 13. The City continues to pay the retiree's share of the single rate premium. The City's contribution for these retired individuals was \$362,250 for the year ended June 30. At June 30, there were 75 participants eligible to receive benefits under this program.

Second, for those eligible retirees age 65 and over participating in the Nationwide Medicare Program, the City provides supplemental healthcare coverage under the Medicare Extended Plus Program and Medicare D, drug plan administered by Anthem Blue Cross Blue Shield. The City's contribution to this program for the year ended June 30 was \$209,307. This amount represents the full single premium for retirees. The City's liability under this program is limited to paying the monthly premium. At June 30, there were 122 participants eligible to receive benefits under this program.

The City's contributions under these two programs are funded on a current disbursement basis.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

11. Service Contracts

The following is a summary of significant service contracts:

Electrical Service

Agreement with American Electric Power Service Corporation to purchase electricity for consumption and resale to City residents effective July 1, 2006 through May 31, 2026 with two possible renewals of five year periods each. An early termination date may become effective under certain circumstances. The rates are recalculated annually based on the supplier's cost.

Agreement with the United States Department of Energy to purchase electricity during American Electric Power's peak usage periods. The agreement requires a 37-month notification prior to cancellation.

Agreement with Blue Ridge Power Agency for billing and power supply related services and partial assignment of contract effective July 1, 2005 through June 30, 2010. The agreement requires a 90-day notification prior to termination.

Water Contract

Agreement dated July 1, 1981, to sell surplus water to Roanoke County, Virginia at a bulk rate determined by a mutually agreed upon formula. The contract is for a term of 30 years and automatically renews for terms of ten years unless 24 months notice of termination is given. The WVWA has assumed this contract from Roanoke County.

Solid Waste Disposal

On July 1, 2006, the City entered an amendment to the July 1, 1998 agreement with Waste Management Inc., extending the contract for disposal of nonhazardous solid waste until June 30, 2016.

Special Services

The following special services are provided by the County of Roanoke, Virginia under an agreement effective July 1, 1973 which can be renewed or terminated at the end of any two-year period with proper notice:

- Social Services – Salem shares in the local costs of providing services to Salem citizens in need qualifying under Federal Regulations. Salem's share is the total cost of services less any applicable Federal or State Grants.
- Agricultural and Home Demonstration Services – Cost is shared based on population.
- Jail Services and Facilities – Cost is shared per prisoner, per day based on total net cost.

12. Property Taxes

The two major sources of property taxes are described below:

Real Estate

The City levies real estate taxes on all real estate within its boundaries, except that exempted by statute, each year as of July 1 on 100% of estimated fair market value of the property. Real estate taxes become a lien on real property the first day of the levy year. The City follows the practice of reassessing all property biannually. Real estate taxes are due in equal semiannual payments on December 5 and June 5 and are considered delinquent after each due date. The tax rate for 2007 was \$1.18 per \$100 of assessed value. Beginning with fiscal year 2008, the City moved to a system of annual reassessments as allowed by state code.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

12. Property Taxes (Continued)

Personal Property

The City levies personal property taxes on motor vehicles and business and other tangible personal property. Personal property taxes do not create a lien on property; however, City vehicle tags, which are required by law for all vehicles garaged in the City, may not be issued to any individual having outstanding personal property taxes. These levies are made each year as of January 1 with payment due the following May 31. In addition, personal property transactions during the year are taxed on a prorated basis. Personal property taxes are considered delinquent after the May 31 due date. The tax rate for 2007 was \$3.20 per \$100 of assessed value.

13. Risk Management

The Risk Management Programs of the City are as follows:

Workers' Compensation

Workers' Compensation Insurance is provided through the Virginia Municipal Self Insurance Association for the City and through School Systems of Virginia for the School Division. Benefits are those afforded through the Commonwealth of Virginia as outlined in the *Code of Virginia* Section 65.2-100; premiums are based upon covered payroll, job rates, and claims experience. Total premiums for the current year were \$416,053 and \$74,391 for the City and School Division, respectively.

General Liability and Other

The City provides general liability and other insurance through policies with the St. Paul Insurance Company. General liability and business automobile have a \$2,000,000 limit. Boiler and machinery coverage and property insurance are covered as per statement of values. The City maintains an additional \$5,000,000 umbrella policy over all forms of liability through the St. Paul Insurance Company. Lastly, both Police Professional Liability and Public Officials Liability Insurance with a \$1,000,000 limit are covered through a policy with the Commonwealth of Virginia. Total premiums for the current year were \$580,003.

Healthcare

The City's professionally administered self-insurance program provides health coverage for employees of the City and the School Division on a cost-reimbursement basis. Retired employees and dependents of employees of the City are also covered by the program provided they pay a premium to the City. Under the program, the City is obligated for claims payments. A stop loss insurance contract executed with an insurance carrier covers claims in excess of \$125,000 per covered individual and approximately \$8,898,818 in the aggregate. During the year ended June 30, total claims expense of \$5,879,714, which did not exceed the stop loss provisions, was incurred. This represents claims processed and an estimate, based on plan experience prior and subsequent to June 30 for claims incurred but not reported (IBNR) as of June 30. The designated portion of fund balance for self-insurance equaled \$610,454 at June 30. The estimated liability at June 30, including reported and IBNR claims, was \$370,380. Changes in the reported liability during the last three fiscal years are as follows:

Year Ended June 30	Liability July 1	Claims and Changes in Estimates	Claim Payments	Liability June 30
2007	\$ 650,201	\$ 5,879,714	\$ 6,159,535	\$ 370,380
2006	\$ 541,469	\$ 6,521,345	\$ 6,412,613	\$ 650,201
2005	\$ 698,955	\$ 5,593,438	\$ 5,750,924	\$ 541,469

Other

There were no significant changes in insurance coverages from the prior year and no settlements that exceeded the amount of insurance coverage during the last three fiscal years.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2007**

14. Commitments and Contingencies

Special Purpose Grants

Special Purpose Grants are subject to audit to determine compliance with their requirements. City officials believe that if any refunds are required, they will be immaterial.

Litigation

Various claims and lawsuits are pending against the City. In the opinion of management, after consulting with legal counsel, the potential loss on all claims and lawsuits will not materially affect the City's financial position.

15. Prior Period Adjustment

During fiscal year 2007, the School Division elected to change its method of recognizing sales tax revenue. Previously only July receipts were accrued, however the policy has been changed to also accrue August receipts. As such, beginning net assets and school operating fund balance have been increased by \$277,000 to record the August 2006 sales tax receipts as of June 30, 2006. This change reflects the School Division's current 60 day period of availability.

16. New Accounting Standards

The Governmental Accounting Standards Board (GASB) has issued its Statement No. 45 *Accounting and Financial Reporting by Employers for Postemployment Benefit Plans Other Than Pensions*. The Statement establishes standards for the measurement, recognition and display of OPEB expense and related liabilities in the financial statements. Management has not completed the process of evaluating the impact that will result from adoption of the standard, and is therefore unable to disclose the impact of adoption. The requirements of the Statement are effective in three phases based on the government's annual revenues, with the earliest effective date being for the year ended June 30, 2008. The City is required to implement this Statement for fiscal year end June 30, 2009.

GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, addresses the accounting and reporting of transactions where an interest in expected cash flows from specific receivables or specific future revenues is exchanged for immediate cash payments, and establishes criteria to determine whether the proceeds received should be a revenue or a liability. The statement also addresses intra-entity transfers of assets (including capital assets), and requires that the transferee should recognize the assets received at the carrying value of the transferor. Management does not believe that the effects of adopting this standard will be material. This statement will be effective for the year ended June 30, 2008.

GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, addresses accounting and financial reporting standards for certain obligations to address the effects of existing pollution through pollution remediation activities such as site assessments and cleanups. The standard excludes pollution prevention or control obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care. Upon the occurrence of certain events, a government is required to estimate expected pollution remediation outlays and determine whether those outlays should be accrued as a liability, or, if appropriate, capitalized when goods and services are received. Management has implemented this standard, in relation to the environmental remediation mentioned in Note 8, but has not assessed the impact of the standard on other potential pollution remediation. The statement will be effective for the year ended June 30, 2009.

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REQUIRED SUPPLEMENTARY INFORMATION

CITY OF SALEM, VIRGINIA
REQUIRED SUPPLEMENTARY INFORMATION
ANALYSIS OF FUNDING PROGRESS FOR DEFINED BENEFIT PENSION PLAN
JUNE 30, 2007

City Employees

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as of Percentage of Covered Payroll ((b-a)/c)
June 30, 2006	\$ 106,097,930	\$ 128,345,085	\$ 22,247,155	82.7%	\$ 33,208,954	67.0%
June 30, 2005	\$ 98,906,486	\$ 123,869,651	\$ 24,963,165	79.8%	\$ 31,283,159	79.8%
June 30, 2004	\$ 95,206,763	\$ 109,456,032	\$ 14,249,269	87.0%	\$ 30,358,747	46.9%

Component Unit - School Board Non-Professional Employees

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as of Percentage of Covered Payroll ((b-a)/c)
June 30, 2006	\$ 3,272,166	\$ 3,308,571	\$ 36,405	98.9%	\$ 1,364,503	2.7%
June 30, 2005	\$ 3,073,833	\$ 3,248,857	\$ 175,024	94.6%	\$ 1,287,079	13.6%
June 30, 2004	\$ 2,980,504	\$ 2,840,773	\$ (139,731)	104.9%	\$ 1,188,646	-11.8%

OTHER SUPPLEMENTARY INFORMATION

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF NET ASSETS
NONMAJOR PROPRIETARY FUNDS
JUNE 30, 2007

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
ASSETS			
<i>Current assets:</i>			
Cash and cash equivalents	\$ 89,160	\$ 250,147	\$ 339,307
Receivables, net	165,427	61,077	226,504
Inventories	-	19,902	19,902
Prepaid items	97,815	-	97,815
Total current assets	<u>352,402</u>	<u>331,126</u>	<u>683,528</u>
<i>Noncurrent assets:</i>			
Capital assets, net	3,154,241	44,967	3,199,208
Total noncurrent assets	<u>3,154,241</u>	<u>44,967</u>	<u>3,199,208</u>
Total assets	<u>3,506,643</u>	<u>376,093</u>	<u>3,882,736</u>
LIABILITIES			
<i>Current liabilities:</i>			
Accounts payable and accrued liabilities	164,681	40,985	205,666
Accrued payroll and related liabilities	81,306	26,578	107,884
Self insurance claims liability	5,611	1,474	7,085
Unearned revenue	101,591	-	101,591
Compensated absences	49,210	13,467	62,677
Total current liabilities	<u>402,399</u>	<u>82,504</u>	<u>484,903</u>
<i>Noncurrent liabilities:</i>			
Compensated absences	11,520	13,273	24,793
Total noncurrent liabilities	<u>11,520</u>	<u>13,273</u>	<u>24,793</u>
Total liabilities	<u>413,919</u>	<u>95,777</u>	<u>509,696</u>
NET ASSETS (DEFICIT)			
Invested in capital assets, net of related debt	3,154,241	44,967	3,199,208
Unrestricted	(61,517)	235,349	173,832
Total net assets	<u>\$ 3,092,724</u>	<u>\$ 280,316</u>	<u>\$ 3,373,040</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
NONMAJOR PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2007

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
OPERATING REVENUES			
Charges for services	\$ 965,194	\$ 1,072,535	\$ 2,037,729
Commissions	30,952	-	30,952
Other	10,198	24,637	34,835
Total operating revenues	<u>1,006,344</u>	<u>1,097,172</u>	<u>2,103,516</u>
OPERATING EXPENSES			
Salaries	1,066,728	382,646	1,449,374
Fringe benefits	327,179	95,029	422,208
Show expenses	171,921	-	171,921
Maintenance	332,969	6,514	339,483
Professional services	16,404	20,834	37,238
Insurance	14,971	-	14,971
Administration	19,579	6,539	26,118
Travel and training	12,004	4,999	17,003
Materials and supplies	57,587	323,043	380,630
Utilities	257,347	160	257,507
Miscellaneous	230	2,894	3,124
Depreciation	286,171	13,599	299,770
Commissions	-	247,603	247,603
Total operating expenses	<u>2,563,090</u>	<u>1,103,860</u>	<u>3,666,950</u>
Operating loss	<u>(1,556,746)</u>	<u>(6,688)</u>	<u>(1,563,434)</u>
NONOPERATING REVENUES (EXPENSES)			
Interest income	555	-	555
Loss on sale of capital assets	(2,044)	(426)	(2,470)
Net nonoperating expenses	<u>(1,489)</u>	<u>(426)</u>	<u>(1,915)</u>
Loss before transfers	<u>(1,558,235)</u>	<u>(7,114)</u>	<u>(1,565,349)</u>
TRANSFERS IN	1,301,018	9,565	1,310,583
TRANSFERS OUT	<u>(95,556)</u>	-	<u>(95,556)</u>
Change in net assets	<u>(352,773)</u>	<u>2,451</u>	<u>(350,322)</u>
NET ASSETS AT JULY 1	3,445,497	277,865	3,723,362
NET ASSETS AT JUNE 30	<u>\$ 3,092,724</u>	<u>\$ 280,316</u>	<u>\$ 3,373,040</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF CASH FLOWS
NONMAJOR PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2007

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
OPERATING ACTIVITIES			
Receipts from customers	\$ 878,458	\$ 1,096,251	\$ 1,974,709
Payments to suppliers	(973,299)	(609,270)	(1,582,569)
Payments to employees	(1,378,632)	(481,270)	(1,859,902)
Other receipts	41,150	24,637	65,787
Net cash provided by (used in) operating activities	<u>(1,432,323)</u>	<u>30,348</u>	<u>(1,401,975)</u>
NONCAPITAL FINANCING ACTIVITIES			
Interfund transfers	1,301,018	-	1,301,018
Net cash provided by noncapital financing activities	<u>1,301,018</u>	<u>-</u>	<u>1,301,018</u>
CAPITAL AND RELATED FINANCING ACTIVITIES			
Purchases of capital assets	(445,543)	(15,908)	(461,451)
Net cash used in capital and related financing activities	<u>(445,543)</u>	<u>(15,908)</u>	<u>(461,451)</u>
INVESTING ACTIVITIES			
Interest received	555	-	555
Net cash provided by investing activities	<u>555</u>	<u>-</u>	<u>555</u>
Net increase (decrease) in cash and cash equivalents	<u>(576,293)</u>	<u>14,440</u>	<u>(561,853)</u>
CASH AND CASH EQUIVALENTS			
Beginning at July 1	665,453	235,707	901,160
Ending at June 30	<u>\$ 89,160</u>	<u>\$ 250,147</u>	<u>\$ 339,307</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES			
Operating loss	\$ (1,556,746)	\$ (6,688)	\$ (1,563,434)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities			
Depreciation and amortization	286,171	13,599	299,770
Change in assets and liabilities			
(Increase) decrease in:			
Receivables, net	(50,432)	(2,496)	(52,928)
Due from other funds	-	26,212	26,212
Inventories	-	7,352	7,352
Prepaid items	(27,942)	-	(27,942)
Accounts payable and accrued liabilities	(33,454)	(2,085)	(35,539)
Accrued payroll and related liabilities	15,275	(3,595)	11,680
Self insurance claims liability	(7,364)	(1,951)	(9,315)
Due to other funds	(21,527)	-	(21,527)
Unearned revenue	(36,304)	-	(36,304)
Net cash provided by (used in) operating activities	<u>\$ (1,432,323)</u>	<u>\$ 30,348</u>	<u>\$ (1,401,975)</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF FIDUCIARY NET ASSETS
JUNE 30, 2007

	Cardinal Criminal Justice Academy	Court- Community Corrections Program	Agency Funds
ASSETS			
Cash and cash equivalents	\$ 324,623	\$ 185,139	\$ 509,762
Grant receivable	1,485	1,006	\$ 2,491
Due from Commonwealth of Virginia	-	104,575	\$ 104,575
Total assets	<u>\$ 326,108</u>	<u>\$ 290,720</u>	<u>\$ 616,828</u>
LIABILITIES			
Accounts payable	\$ 1,539	\$ 71,598	\$ 73,137
Liability to agency	324,569	219,122	\$ 543,691
Total liabilities	<u>\$ 326,108</u>	<u>\$ 290,720</u>	<u>\$ 616,828</u>

CITY OF SALEM, VIRGINIA
 COMBINING STATEMENT OF CHANGES IN FIDUCIARY ASSETS AND LIABILITIES
 JUNE 30, 2007

	Cardinal Criminal Justice Academy	Court- Community Corrections Program	Agency Funds
ASSETS			
Balance, Beginning of Year	\$ 312,422	\$ 224,791	\$ 537,213
Additions	584,698	2,059,756	2,644,454
Deletions	571,012	1,993,827	2,564,839
Balance, End of Year	<u>\$ 326,108</u>	<u>\$ 290,720</u>	<u>\$ 616,828</u>
LIABILITIES			
Balance, Beginning of Year	\$ 312,422	\$ 224,791	\$ 537,213
Additions	584,698	2,059,756	2,644,454
Deletions	571,012	1,993,827	2,564,839
Balance, End of Year	<u>\$ 326,108</u>	<u>\$ 290,720</u>	<u>\$ 616,828</u>

STATISTICAL SECTION

This part of the City of Salem, Virginia's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the government's overall health.

Contents	Page
Financial Trends.....	71
<i>These schedules contain trend information to help the reader understand how the government's financial performance and well-being have changed over time.</i>	
Revenue Capacity.....	77
<i>These schedules contain information to help the readers assess the government's most significant local revenue sources, the property tax and sale of electricity.</i>	
Debt Capacity.....	80
<i>These schedules present information to help the reader assess the affordability of the government's current level of outstanding debt and the government's ability to issue additional debt in the future.</i>	
Demographic and Economic Information.....	82
<i>These schedules offer demographic and economic indicators to help the reader understand the environment within which the government's financial activities take place.</i>	
Operating Information.....	85
<i>These schedules contain service and infrastructure data to help the reader understand how the information in the government's financial report relates to the services the government provides and the activities it performs.</i>	

TABLE 1
UNAUDITED

CITY OF SALEM, VIRGINIA
NET ASSETS BY COMPONENT
LAST FIVE FISCAL YEARS

	<u>2007</u>	<u>2006*</u>	<u>2005*</u>	<u>2004*</u>	<u>2003*</u>
Governmental Activities					
Invested in capital assets, net of related debt	\$ 85,853,628	\$ 88,112,343	\$ 89,479,130	\$ 88,551,933	\$ 76,959,696
Restricted	-	-	-	2,313,457	2,473,586
Unrestricted	(9,132,365)	(12,509,444)	(12,674,607)	(15,644,583)	(3,239,660)
Total governmental net assets	<u>\$ 76,721,263</u>	<u>\$ 75,602,899</u>	<u>\$ 76,804,523</u>	<u>\$ 75,220,807</u>	<u>\$ 76,193,622</u>
Business-type activities					
Invested in capital assets, net of related debt	\$ 41,636,232	\$ 36,954,684	\$ 36,501,799	\$ 31,689,583	\$ 23,078,380
Unrestricted	20,767,546	21,804,567	21,839,306	24,685,946	31,038,458
Total business-type activities net assets	<u>\$ 62,403,778</u>	<u>\$ 58,759,251</u>	<u>\$ 58,341,105</u>	<u>\$ 56,375,529</u>	<u>\$ 54,116,838</u>
Primary government					
Invested in capital assets, net of related debt	\$ 127,489,860	\$ 125,067,027	\$ 125,980,929	\$ 120,241,516	\$ 100,038,076
Restricted	-	-	-	2,313,457	2,473,586
Unrestricted	11,635,181	9,295,123	9,164,699	9,041,363	27,798,798
Total primary government net assets	<u>\$ 139,125,041</u>	<u>\$ 134,362,150</u>	<u>\$ 135,145,628</u>	<u>\$ 131,596,336</u>	<u>\$ 130,310,460</u>

Source: City of Salem Finance Department

Notes:

Information is presented beginning with FY03, the year the City implemented GASB 34.

*Invested in capital assets, net of related debt and unrestricted net assets of governmental activities were restated to properly classify School Division debt.

**TABLE 2
UNAUDITED**

**CITY OF SALEM, VIRGINIA
CHANGES IN NET ASSETS
LAST FIVE FISCAL YEARS
(accrual basis of accounting)**

Expenses	2007	2006	2005	2004	2003
<i>Governmental activities</i>					
General government	\$ 4,803,246	\$ 5,107,268	\$ 4,283,754	\$ 4,402,755	\$ 4,156,677
Judicial administration	1,540,762	1,457,720	1,292,722	1,224,425	1,190,643
Public safety	13,869,676	13,547,191	11,535,321	10,574,969	10,409,689
Public works	13,476,019	12,443,334	10,789,008	9,603,482	9,471,217
Health and welfare	2,193,126	2,055,166	1,823,783	1,419,802	1,217,958
Education	17,095,000	16,266,005	15,618,081	29,340,564	(1) 14,747,635
Parks, recreation and cultural	5,796,220	5,239,517	3,851,575	4,257,005	3,697,241
Community development	1,022,096	933,002	513,272	842,963	1,290,922
Nondepartmental	-	-	2,424,022	1,788,744	2,253,821
Interest on long-term debt	1,202,201	1,267,296	1,478,103	1,339,037	1,045,306
Total governmental activities	<u>60,998,346</u>	<u>58,316,499</u>	<u>53,609,641</u>	<u>64,793,746</u>	<u>49,481,109</u>
<i>Business-type activities</i>					
Electric	24,218,848	24,692,031	16,311,434	15,116,855	16,810,659
Water and sewage	11,073,841	10,836,280	9,502,885	7,305,334	7,427,270
Civic Center	2,563,090	2,364,891	2,199,589	2,096,344	1,856,562
Catering and concessions	1,103,860	1,036,737	960,320	953,609	932,823
Total business-type activities expense	<u>38,959,639</u>	<u>38,929,939</u>	<u>28,974,228</u>	<u>25,472,142</u>	<u>27,027,314</u>
Total primary government expenses	<u>\$ 99,957,985</u>	<u>\$ 97,246,438</u>	<u>\$ 82,583,869</u>	<u>\$ 90,265,888</u>	<u>\$ 76,508,423</u>
Program Revenues					
<i>Governmental activities</i>					
Charges for services					
Public safety	\$ 1,148,627	\$ 1,315,417	\$ 1,083,694	\$ 532,717	\$ 553,437
Public works	2,892,913	1,799,284	1,821,717	1,805,400	1,781,202
Other activities	535,125	471,137	415,225	508,282	426,281
Operating grants and contributions	7,024,034	6,038,168	5,979,520	5,359,113	5,557,143
Capital grants and contributions	1,168,709	6,392,874	314,789	3,260,581	300,000
Total governmental activities program revenues	<u>12,769,408</u>	<u>16,016,880</u>	<u>9,614,945</u>	<u>11,466,093</u>	<u>8,618,063</u>
<i>Business-type activities</i>					
Charges for services					
Electric	29,300,625	27,699,386	20,192,965	20,092,111	19,640,717
Water and sewage	10,740,194	9,529,125	8,510,106	8,368,156	7,663,093
Civic Center	1,006,344	793,716	887,312	862,129	716,643
Catering and concessions	1,097,172	991,208	967,446	975,666	995,280
Total business-type activities program revenues	<u>42,144,335</u>	<u>39,013,435</u>	<u>30,557,829</u>	<u>30,298,062</u>	<u>29,015,733</u>
Total primary government program revenues	<u>\$ 54,913,743</u>	<u>\$ 55,030,315</u>	<u>\$ 40,172,774</u>	<u>\$ 41,764,155</u>	<u>\$ 37,633,796</u>
Net (expense) revenue					
Governmental activities	\$ (48,228,938)	\$ (42,299,619)	\$ (43,994,696)	\$ (53,327,653)	\$ (40,863,046)
Business-type activities	3,184,696	83,496	1,583,601	4,825,920	1,988,419
Total primary government net expense	<u>\$ (45,044,242)</u>	<u>\$ (42,216,123)</u>	<u>\$ (42,411,095)</u>	<u>\$ (48,501,733)</u>	<u>\$ (38,874,627)</u>

(Continued)

**TABLE 2
(Continued)**

CITY OF SALEM, VIRGINIA CHANGES IN NET ASSETS LAST FIVE FISCAL YEARS (accrual basis of accounting)					
	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
General Revenues and Other Changes in Net Assets					
<i>Governmental activities:</i>					
Taxes					
Property taxes	\$ 27,606,560	\$ 27,161,942	\$ 25,062,245	\$ 24,868,585	\$ 23,353,997
Meals tax	2,397,412	2,351,010	2,190,099	2,091,998	2,055,706
Local sales and use taxes	5,711,940	5,634,585	5,601,846	5,397,710	4,996,579
Utility taxes	1,228,975	1,372,250	1,339,238	1,122,167	1,141,696
Business license tax	4,258,059	3,866,585	4,032,843	3,647,786	3,496,933
Other taxes	2,700,657	2,625,066	2,486,633	2,484,614	2,233,301
Intergovernmental revenue not restricted	3,878,955	3,523,634	3,597,191	3,213,462	3,243,932
Unrestricted investment earnings	789,526	556,039	501,808	394,977	319,062
Gain (loss) on sale of property	-	402,089	571,311	-	-
Other	279,223	218,274	266,019	285,750	302,877
Transfers	495,995	975,685	(70,821)	236,756	226,527
Total governmental activities	<u>49,347,302</u>	<u>48,687,159</u>	<u>45,578,412</u>	<u>43,743,805</u>	<u>41,370,610</u>
<i>Business-type activities:</i>					
Unrestricted investment earnings	928,710	271,303	311,154	110,832	369,743
Gain (loss) on sale of property	6,967	-	-	-	-
Other	20,149	-	-	-	-
Transfers	(495,995)	(975,685)	70,821	(236,756)	(226,527)
Total business-type activities	<u>459,831</u>	<u>(704,382)</u>	<u>381,975</u>	<u>(125,924)</u>	<u>143,216</u>
Total primary government	<u>\$ 49,807,133</u>	<u>\$ 47,982,777</u>	<u>\$ 45,960,387</u>	<u>\$ 43,617,881</u>	<u>\$ 41,513,826</u>
Changes in Net Assets					
Governmental activities	\$ 1,118,364	\$ 6,387,540	\$ 1,965,576	\$ 4,699,996	\$ 2,131,635
Business-type activities	3,644,527	(620,886)	1,583,716	(9,583,848)	507,564
Total primary government	<u>\$ 4,762,891</u>	<u>\$ 5,766,654</u>	<u>\$ 3,549,292</u>	<u>\$ (4,883,852)</u>	<u>\$ 2,639,199</u>

Source: City of Salem Finance Department

Notes:

Information is presented beginning with FY03, the year the City implemented GASB 34.

(1) This amount includes \$14,000,000 of bond funds transferred to the School Division to fund capital projects.

TABLE 3
UNAUDITED

CITY OF SALEM, VIRGINIA
FUND BALANCES, GOVERNMENTAL FUNDS
LAST TEN FISCAL YEARS

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
General Fund										
Reserved	\$ 1,357,034	\$ 1,431,926	\$ 1,179,343	\$ 1,009,767	\$ 745,321	\$ 811,145	\$ 967,680	\$ 857,533	\$ 839,548	\$ 1,006,052
Unreserved	6,547,440	6,419,834	10,534,365	11,124,617	10,319,757	7,785,113	8,494,384	8,290,010	5,540,300	4,715,564
Total General Fund	<u>\$ 7,904,474</u>	<u>\$ 7,851,760</u>	<u>\$ 11,713,708</u>	<u>\$ 12,134,384</u>	<u>\$ 11,065,078</u>	<u>\$ 8,596,258</u>	<u>\$ 9,462,064</u>	<u>\$ 9,147,543</u>	<u>\$ 6,379,848</u>	<u>\$ 5,721,616</u>
All Other Governmental Funds										
Reserved	\$ 1,083,915	\$ 1,251,705	\$ 3,777,959	\$ 7,434,079	\$ 2,920,546	\$ 2,639,011	\$ 702,166	\$ 980,723	\$ 1,569,842	\$ -
<i>Unreserved, reported in:</i>										
Debt service fund	-	-	-	-	-	-	-	-	-	-
Capital projects fund	(189,129)	(463,348)	(1,691,345)	2,914,998	(305,531)	-	-	-	-	29,933
Total all other governmental funds	<u>\$ 894,786</u>	<u>\$ 788,357</u>	<u>\$ 2,086,614</u>	<u>\$ 10,349,077</u>	<u>\$ 2,615,015</u>	<u>\$ 2,639,011</u>	<u>\$ 702,166</u>	<u>\$ 980,723</u>	<u>\$ 1,569,842</u>	<u>\$ 29,933</u>

Source: City of Salem Finance Department

TABLE 4
UNAUDITED

CITY OF SALEM, VIRGINIA
CHANGES IN FUND BALANCE, GOVERNMENTAL FUNDS
LAST TEN FISCAL YEARS

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Revenue										
Taxes	\$ 44,555,391	\$ 44,037,357	\$ 41,593,054	\$ 40,747,374	\$ 38,137,448	\$ 36,436,995	\$ 35,323,279	\$ 35,547,144	\$ 34,505,383	\$ 33,727,514
Permits, privilege fees, and regulatory licenses	293,004	294,314	286,150	308,511	257,796	269,237	237,722	268,517	244,810	245,138
Fines and forfeitures	159,363	150,860	162,207	197,297	170,922	156,128	159,404	162,188	117,048	108,977
Revenue from use of money and property	1,434,893	1,385,122	1,861,432	579,303	482,878	928,857	1,197,369	1,103,489	712,303	439,550
Charges for services	3,915,569	2,959,842	2,749,670	2,186,113	2,168,506	1,967,128	1,950,211	2,146,002	1,955,586	2,149,051
Other	47,673	32,544	43,796	53,590	385,733	1,385,165	1,142,483	1,099,482	917,618	900,645
Intergovernmental	10,336,870	8,720,129	8,765,664	7,764,376	8,562,593	8,400,270	7,663,260	7,146,529	4,612,946	4,611,127
Total revenues	60,742,763	57,580,168	55,461,973	51,836,564	50,165,876	49,543,780	47,673,728	47,473,351	43,065,694	42,182,002
Expenditures										
General government administration	4,694,442	4,994,542	4,386,061	4,005,851	3,555,873	3,330,674	3,511,823	3,145,638	2,876,123	2,600,765
Judicial administration	1,506,395	1,321,052	1,256,107	1,207,990	1,172,370	1,185,883	1,152,094	1,090,282	1,036,931	1,039,647
Public safety	13,358,739	12,707,985	11,670,171	10,740,352	10,103,738	9,706,080	9,058,667	8,610,382	8,215,706	7,515,791
Public works	11,434,040	9,400,116	9,777,021	8,879,090	8,514,725	9,491,691	8,036,110	7,791,651	7,957,248	8,471,332
Health and welfare	2,163,687	1,918,490	1,823,783	1,419,802	1,217,958	1,858,199	1,541,957	1,455,984	1,324,350	1,234,790
Education	17,095,000	16,266,005	15,618,081	15,340,564	14,747,635	14,851,000	15,552,599	15,005,469	14,274,284	13,777,388
Parks, recreation, and cultural	4,354,144	4,316,920	4,037,410	3,696,621	3,336,510	3,549,487	3,238,115	3,136,048	2,831,101	2,599,727
Community development	639,535	815,991	513,272	842,963	1,290,922	843,615	662,157	508,435	337,914	223,287
Non-departmental	1,769,127	3,610,694	2,424,022	1,788,744	2,253,821	1,669,551	1,163,257	2,002,046	1,343,146	1,507,441
Capital projects	2,750,335	4,325,562	5,519,655	14,604,233	76,230	819,507	1,379,692	589,119	459,386	-
<i>Debt service:</i>										
Principal retirement	2,607,365	2,863,024	5,616,505 (1)	1,055,518	1,628,985	1,969,433	903,164	944,572	900,553	859,716
Interest and fiscal charges	1,119,793	1,185,708	1,432,203	1,150,476	1,063,168	1,160,076	430,350	481,247	447,130	510,306
Total expenditures	63,492,602	63,726,089	64,074,291	64,732,204	48,961,935	50,435,196	46,629,985	44,760,873	42,003,872	40,340,190
Excess of revenues over (under) expenditures	(2,749,839)	(6,145,921)	(8,612,318)	(12,895,640)	1,203,941	(891,416)	1,043,743	2,712,478	1,061,822	1,841,812
Other Financing Sources (Uses)										
Proceeds from borrowing	-	-	-	31,970,540	-	-	-	-	2,000,000	428,145
Payments to bond escrow agents	-	-	-	(10,508,287)	-	-	-	-	-	-
Transfers in	7,536,323	8,235,360	5,417,206	4,252,823	3,993,355	2,862,517	2,189,014	1,825,819	1,443,662	1,390,258
Transfers out	(4,627,341)	(7,249,644)	(5,488,027)	(4,016,067)	(3,766,828)	(3,875,163)	(3,196,793)	(2,359,721)	(2,307,343)	(2,607,419)
Total other financing sources (uses)	2,908,982	985,716	(70,821)	21,699,009	226,527	(1,012,646)	(1,007,779)	(533,902)	1,136,319	(789,016)
Net change in fund balances	\$ 159,143	\$ (5,160,205)	\$ (8,683,139)	\$ 8,803,369	\$ 1,430,468	\$ (1,904,062)	\$ 35,964	\$ 2,178,576	\$ 2,198,141	\$ 1,052,796
Debt service as a percentage of noncapital expenditures	6.70%	7.06%	12.35% (2)	4.60%	5.68%	6.51%	3.09%	3.36%	3.36%	3.50%

Source: City of Salem Finance Department

Notes:

(1) Includes one-time balloon payment of \$2,715,000.

(2) Net of balloon payment, percentage equals 7.59%.

**TABLE 5
UNAUDITED**

**CITY OF SALEM
ASSESSED VALUE AND ACTUAL VALUE OF TAXABLE PROPERTY
LAST TEN FISCAL YEARS**

Fiscal Year Ended June 30,	Real Estate	Personal Property	Machinery and Tools	Public Service Corporation	Mobile Homes	Total Taxable Assessed Value	Total Direct Tax Rate
2007	\$ 1,601,239,600	\$ 254,765,656	\$ 86,685,532	\$ 36,451,099	\$ 1,632,022	\$ 1,980,773,909	\$ 1.52
2006	1,572,732,200	262,141,563	86,409,864	34,992,259	1,855,348	1,958,131,234	1.54
2005	1,414,891,600	253,619,878	82,714,938	33,586,047	2,186,076	1,786,998,539	1.55
2004	1,386,790,100	250,218,290	88,317,031	35,032,203	2,092,797	1,762,450,421	1.56
2003	1,276,162,600	262,415,563	75,075,156	35,658,160	2,257,457	1,651,568,936	1.60
2002	1,260,133,200	257,336,535	81,289,685	36,825,471	2,573,480	1,638,158,371	1.60
2001	1,159,955,100	291,662,164	79,003,832	35,119,042	2,782,250	1,568,522,388	1.66
2000	1,132,465,500	252,607,101	87,609,659	33,842,393	3,311,164	1,509,835,817	1.65
1999	1,035,946,400	234,113,024	83,530,905	30,630,006	3,508,695	1,387,729,030	1.64
1998	1,014,195,800	218,922,343	83,591,859	31,223,785	3,799,229	1,351,733,016	1.64

Source: City of Salem Finance Department

TABLE 6
UNAUDITED

CITY OF SALEM, VIRGINIA
PRINCIPAL PROPERTY TAXPAYERS
CURRENT YEAR AND NINE YEARS AGO

Taxpayer	2007			1998		
	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value
Lewis-Gale Hospital HCA	\$ 63,017,000	1	3.52%	\$ 19,729,200	2	(1) 1.90%
Yokohama Industries	16,327,300	2	0.91%	13,811,500	3	1.33%
U.S. Food Service, Inc.	12,364,000	3	0.69%	5,302,200	9	0.51%
General Electric	10,536,100	4	0.59%	10,700,700	4	1.03%
C. S. W. Associates/Chateau Riviera Apartments	8,394,300	5	0.47%	6,962,900	7	0.67%
Spartan Square, Inc.	7,923,700	6	0.44%			
Rowe Furniture/Salem Frame	7,365,400	7	0.41%	7,766,400	6	0.75%
Wal-Mart, Inc.	6,840,900	8	0.38%	5,680,500	8	0.55%
Carthy Corporation/Carter Machinery	6,525,300	9	0.36%			
Lakeside Plaza	5,818,500	10	0.33%			
Lewis-Gale Building Corporation				19,786,600	1	(1) 1.91%
Home Shopping/Stuart McGuire				8,662,400	5	0.84%
Willow River Associates				5,256,000	10	0.51%

Source: City of Salem Real Estate Valuation Department.

Note:

(1) In 2005, Lewis-Gale Hospital HCA acquired the assets of Lewis-Gale Building Corporation.

TABLE 7
UNAUDITED

CITY OF SALEM, VIRGINIA
PRINCIPAL ELECTRIC CUSTOMERS
CURRENT YEAR AND NINE YEARS AGC

Customer	2007			1998		
	Services Billed	Rank	Percentage of Total Services Billed	Services Billed	Rank	Percentage of Total Services Billed
Lewis-Gale Hospital HCA	\$ 1,282,234	1	4.44%	\$ 737,541	1	3.98%
Roanoke College	895,320	2	3.10%	462,045	4	2.49%
Graham White	689,692	3	2.39%	468,534	3	2.53%
U.S. Food Service, Inc.	591,739	4	2.05%			
Rowe Furniture/Salem Frame	547,662	5	1.90%	524,693	2	2.83%
Old Virginia Brick	427,195	6	1.48%	201,855	8	1.09%
Kroger	423,501	7	1.47%	310,558	7	1.68%
Carter Machinery	340,576	8	1.18%	183,343	9	0.99%
Sewell Products	315,838	9	1.09%			
Wal-Mart	253,267	10	0.88%	167,693	10	0.90%
Valleydale				324,058	6	1.75%
Home Shopping Network				352,448	5	1.90%

Source: City of Salem Finance Department

**TABLE 8
UNAUDITED**

**CITY OF SALEM, VIRGINIA
PROPERTY TAX LEVIES AND COLLECTIONS
LAST TEN FISCAL YEARS**

Fiscal Year	Taxes Levied for the Fiscal Year	Collected within the Fiscal Year of the Levy		Collections in Subsequent Year	Total Collections to Date	
		Amount (1)	Percentage of Levy		Amount	Percentage of Levy
2007	\$ 30,693,167	\$ 29,855,379	97.27%	\$ 455,608	\$ 30,310,987	98.75%
2006	30,146,687	29,379,690	97.46%	273,850	29,653,540	98.36%
2005	27,797,041	27,074,619	97.40%	294,662	27,369,281	98.46%
2004	27,635,328	26,861,320	97.20%	364,687	27,226,007	98.52%
2003	26,305,825	25,829,614	98.19%	253,199	26,082,813	99.15%
2002	25,816,066	25,015,942	96.90%	259,718	25,275,660	97.91%
2001	24,642,171	24,300,445	98.61%	255,210	24,555,655	99.65%
2000	24,340,279	24,089,227	98.97%	239,461	24,328,688	99.95%
1999	22,512,879	22,294,549	99.03%	236,974	22,531,523	100.08%
1998	21,754,573	21,513,420	98.89%	644,141	22,157,561	101.85%

Source: City of Salem Finance Department

Note:

(1) Includes state share of personal property taxes.

TABLE 9
UNAUDITED

CITY OF SALEM, VIRGINIA
RATIOS OF GENERAL BONDED DEBT OUTSTANDING
LAST TEN FISCAL YEARS

Fiscal Year	Governmental Activities (1)				Less: Amounts Restricted to Repaying Principal	Total	Percentage of Estimated Actual Value of Taxable Property	Net Bonded Debt Per Capita
	General Obligation Bonds	Loans/ Notes	Capital Leases					
2007	\$ 31,515,845	\$ 500,000	\$ -	\$ -	\$ 32,015,845	1.62%	\$ 1,273.35	
2006	31,498,210	625,000	-	-	32,123,210	1.64%	1,279.81	
2005	34,236,234	750,000	-	-	34,986,234	1.96%	1,393.87	
2004	39,727,739	875,000	-	2,988,308	37,614,431	2.13%	1,520.39	
2003	18,362,717	1,000,000	-	2,673,586	16,689,131	1.01%	675.67	
2002	19,866,702	1,125,000	-	2,621,352	18,370,350	1.12%	740.05	
2001	21,368,934	1,592,200	-	2,737,447	20,223,687	1.29%	817.22	
2000	22,829,000	2,059,400	-	2,769,188	22,119,212	1.47%	897.08	
1999	24,369,864	2,538,200	-	2,759,842	24,148,222	1.74%	980.68	
1998	20,711,349	3,057,000	20,361	2,823,012	20,965,698	1.55%	852.89	

Fiscal Year	Business-Type Activities			Total Primary Government
	General Obligation Bonds	Revenue Bonds (2)	Total	
2007	\$ 54,149,155	\$ 10,801,961	\$ 64,951,116	\$ 96,966,961
2006	58,826,790	8,028,942	66,855,732	98,978,942
2005	36,033,766	4,461,586	40,495,352	75,481,586
2004	39,347,261	432,388	39,779,649	77,394,080
2003	42,047,283	-	42,047,283	58,736,414
2002	45,158,298	-	45,158,298	63,528,648
2001	24,726,065	-	24,726,065	44,949,752
2000	27,190,998	-	27,190,998	49,310,210
1999	29,540,134	-	29,540,134	53,688,356
1998	19,193,650	-	19,193,650	40,159,348

Source: City of Salem Finance Department

Note:

Details regarding the City's outstanding debt can be found in the notes to the financial statements.

See Table 10 for personal income and population data.

(1) Outstanding debt for School Division is included with Governmental Activities.

(2) Represents bonds issued through Virginia Resource Authority for regional sewer improvements.

**TABLE 10
UNAUDITED**

**CITY OF SALEM, VIRGINIA
LEGAL DEBT MARGIN INFORMATION
LAST FIVE FISCAL YEARS**

	<u>2007 (1)</u>	<u>2006 (2)</u>	<u>2005 (3)</u>	<u>2004 (4)</u>	<u>2003 (5)</u>
Assessed Value of Real Property	\$ 1,637,690,699	\$ 1,607,724,459	\$ 1,448,477,647	\$ 1,421,822,303	\$ 1,419,380,260
Debt Limit, 10% of Assessed Value	163,769,070	160,772,446	144,847,765	142,182,230	141,938,026
Amount of Debt Applicable to Limit					
General Obligation Bonds	85,665,000	90,325,000	70,270,000	79,075,000	60,410,000
Other Long Term Debt	11,301,961	8,653,942	5,211,586	1,307,388	1,000,000
Less: Enterprise Fund Bonds (6)	(64,951,116)	(66,855,732)	(40,495,352)	(39,347,261)	(42,047,283)
Less: Resources Restricted to Paying Principal	-	-	-	(2,313,457)	(2,673,586)
Total net debt applicable to limit (7)	<u>32,015,845</u>	<u>32,123,210</u>	<u>34,986,234</u>	<u>38,721,670</u>	<u>16,689,131</u>
Legal Debt Margin	<u>\$ 131,753,225</u>	<u>\$ 128,649,236</u>	<u>\$ 109,861,531</u>	<u>\$ 103,460,560</u>	<u>\$ 125,248,895</u>
Total net debt applicable to the limit as a percentage of debt limit	19.55%	19.98%	24.15%	27.23%	11.76%

Source: City of Salem Finance Department

Notes:

- (1) Includes \$1,601,239,600 in General Real Estate and \$36,451,099 in Public Service Corporation Real Estate.
- (2) Includes \$1,572,732,200 in General Real Estate and \$34,992,259 in Public Service Corporation Real Estate.
- (3) Includes \$1,414,891,600 in General Real Estate and \$33,586,047 in Public Service Corporation Real Estate.
- (4) Includes \$1,386,790,100 in General Real Estate and \$35,032,203 in Public Service Corporation Real Estate.
- (5) Includes \$1,384,722,100 in General Real Estate and \$35,658,160 in Public Service Corporation Real Estate.
- (6) The Enterprise Fund bonds are backed by the full faith and credit of the City but are expected to be paid from the revenue and receipts of the Enterprise Funds.
- (7) School debt is included in the amount of debt applicable to limit

TABLE 11
UNAUDITED

CITY OF SALEM, VIRGINIA
DEMOGRAPHIC AND ECONOMIC INFORMATION
LAST TEN FISCAL YEARS

<u>Fiscal Year Ended (1)</u>	<u>Population (2)</u>	<u>Total Personal Income (In Thousands) (3)</u>	<u>Per Capita Personal Income (4)</u>	<u>Public School Enrollment</u>	<u>Unemployment Rate (5)</u>
2007	25,143	\$ 3,986,137 (est.)	\$ 35,140 (est.)	3,946	3.00%
2006	25,100	3,986,137 (est.)	34,632	3,908	2.90%
2005	25,100	3,986,137	34,632	3,882	2.50%
2004	24,740	3,853,327	33,998	3,888	2.70%
2003	24,700	3,669,268	32,703	3,910	3.80%
2002	24,823	3,654,128	32,795	3,981	3.10%
2001	24,747	3,577,363	32,070	3,889	2.20%
2000	24,657	3,362,886	30,451	3,957	1.60%
1999	24,624	3,215,891	29,688	3,912	1.70%
1998	24,582	3,178,079	29,486	3,920	2.50%

Notes:

- (1) Population, school enrollment and unemployment figures are based on fiscal years ending June 30. Per Capita Income is as of December 31.
- (2) Population is based on figures available from the Weldon Cooper Center, University of Virginia
- (3) Total personal income reported is for Roanoke County and the City of Salem. No data is available for the City of Salem only.
- (4) Source: City Planning Department
- (5) Virginia Employment Commission

TABLE 12
UNAUDITED

CITY OF SALEM, VIRGINIA
PRINCIPAL EMPLOYERS
CURRENT YEAR AND NINE YEARS AGO

Employer	2007			1998		
	Employees	Rank	Percentage of Total City Employment (1)	Employees	Rank	Percentage of Total City Employment (1)
Veterans Administration Medical Center	1,393	1	6.16%	1,353	3	5.28%
Lewis-Gale Hospital HCA	1,344	2	5.94%	1,413	2	5.52%
General Electric	1,100	3	4.86%	1,525	1	5.95%
Virginia Department of Transportation	945	4	4.18%			
Yokohama Industries	900	5	3.98%	980	5	3.83%
City of Salem Schools	581	6	2.57%	490	8	1.91%
City of Salem	531	7	2.35%	480	9	1.87%
U.S. Food Service, Inc.	459	8	2.03%			
Roanoke College	449	9	1.98%	430	10	1.68%
Lewis-Gale Physicians LLC	390	10	1.72%	1,190	4	4.65%
Rowe Furniture				725	6	2.83%
Home Shopping Network				625	7	2.44%

Source: City of Salem Department of Planning and Economic Development, Virginia Employment Commission

Note:

(1) Calculated using data provided by Virginia Employment Commission

**TABLE 13
UNAUDITED**

**CITY OF SALEM, VIRGINIA
FULL-TIME EQUIVALENT CITY GOVERNMENT EMPLOYEES BY FUNCTION/PROGRAM
LAST FIVE FISCAL YEARS**

Program/Function	2007	2006	2005	2004	2003
General government	74	72	72	71	70
Judicial administration	20	19	19	19	19
Public safety	164	162	159	154	154
Public works	111	115	115	114	115
Parks, recreation and cultural	25	25	20	22	22
Community development	3	4	2	2	2
Electric	29	28	29	29	28
Water and sewage	59	58	60	63	63
Civic Center	19	19	20	20	19
Catering and concessions	5	5	5	5	5
Total	509	507	501	499	497

Source: City of Salem Finance Department

CITY OF SALEM, VIRGINIA
OPERATING INDICATORS BY FUNCTION/PROGRAM
LAST FIVE FISCAL YEARS

Program/Function	2007	2006	2005	2004	2003
General government					
Finance					
Accounts payable checks issued	14,617	15,638	16,307	16,836	16,183
Human resources					
Positions filled (full-time and temporary)	201	246	233	219	246
Registrar					
Number of registered voters	15,524	14,995	15,652	15,146	14,442
Fleet					
Pieces of equipment maintained	558	527	517	510	498
Judicial administration					
Sheriff					
Inmates housed	1,296	1,125	1,067	1,497	1,708
Inmate transports	1,427	1,391	1,315	1,471	1,292
Courts worked	639	611	593	588	580
Public safety					
Police					
Calls for service	33,776	30,163	30,442	31,566	30,396
Accidents	1,329	1,221	1,263	1,258	1,221
DUI Arrests	176	159	124	196	254
Fire					
Emergency responses - fire	2,715	3,006	2,537	2,182	2,106
Emergency responses - medic units	2,982	3,289	2,934	2,281	2,007
Hazardous materials responses	146	82	101	72	79
Building inspections					
Residential construction permits issued	336	309	319	272	599
Commercial construction permits issued	93	92	139	163	53
Public works					
Refuse collection					
Refuse collected (tons per year)	90,405	81,379	84,270	92,665	90,762
Tons recycled	4,724	2,154	3,594	3,550	3,559
Other public works					
Tons of asphalt used in resurfacing	14,510	9,111	11,966	8,005	7,088
Square yards of milling completed	84,386	58,605	25,480	17,973	15,990
Tons of salt used	277	901	705	1,350	1,574
Leaves collected (loads)	421	422	604	375	400
Parks, recreation and cultural					
Parks and recreation					
Tournaments hosted	57	59	54	51	54
Special events held	25	21	18	18	18
Youth sports teams	186	184	219	219	214
Adult sports teams	48	40	40	40	42
Library					
Circulation	241,816	233,852	232,892	224,712	230,848
Children's program attendance	4,591	3,580	4,164	2,622	3,324
Patron visits to the library	234,379	228,560	217,477	220,571	214,911
New patrons	1,694	1,510	1,537	1,492	1,553
Internet sessions	55,689	32,650	25,834	27,973	25,845
Electric					
Number of customer accounts	13,032	12,968	12,856	12,883	12,678
Water					
Number of customer accounts	9,170	9,107	9,055	9,035	8,916
Million gallons sold to customers	1,043.4	1,089.5	1,097.3	1,097.7	1,066.3
Sewage					
Number of customer accounts	8,561	8,513	8,461	8,446	8,339
Waste/water treated (million gallons per day)	8.1	6.8	9.2	7.3	7.8
Civic Center					
Concerts	13	6	8	12	16
Meetings	1,081	1,209	1,282	1,259	1,282
Tickets sold	147,491	163,972	129,248	150,801	162,263
Arena utilization days	201	175	203	180	175

Source: Various City Departments

CITY OF SALEM, VIRGINIA
CAPITAL ASSET STATISTICS BY FUNCTION/PROGRAM
LAST FOUR FISCAL YEARS

Program/Function	2007	2006	2005	2004
Public safety				
Police stations	1	1	1	1
Law enforcement vehicles	48	45	42	56
Fire stations	3	3	3	3
Fire trucks	6	5	5	5
Ambulance	5	4	3	3
Public works				
Primary streets (lane miles)	67.5	64.8	64.8	64.3
Secondary streets (lane miles)	269.8	224.8	224.8	222.8
Alley (lane miles)	12	10.8	10.8	10.8
Number of garbage trucks	13	10	11	12
Parks, recreation and cultural				
Community centers	1	3	3	3
Parks/athletic fields	15	15	15	15
Acres of parks maintained	495	495	495	495
Libraries	1	1	1	1
Golf courses	1	1	1	1
Electric				
Substations	11	7	7	7
Miles of distribution lines				
Overhead	158	159	161	161
Underground	33	33	31	31
Miles of transmission lines	17	23	23	23
Water and sewage				
Water treatment plants	1	1	2	2
Miles of distribution lines	181	181	180	155
Miles of sanitary sewers	176	174	174	144

Source: City of Salem Finance Department

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COMPLIANCE SECTION

**CITY OF SALEM, VIRGINIA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2007**

<u>Federal Grantor/Pass-through Grantor</u> <u>(Commonwealth of Virginia)/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
<u>Department of Agriculture</u>		
<i>Department of Agriculture and Consumer Services</i>		
Food Distribution – Commodities – Pass-through Payments	10.555	\$ 103,154
<i>Department of Education</i>		
National School Breakfast Program	10.553	79,999
National School Lunch Program	10.555	370,209
<u>Department of Justice</u>		
<i>Department of Criminal Justice Services</i>		
Crime Victim Assistance	16.588	41,618
<i>Direct Payments</i>		
Drug Enforcement Task Force	16.500	144,276
Homeland Security	97.067	35,296
<u>Department of Transportation</u>		
<i>Division of Motor Vehicles</i>		
State and Highway Safety Program	20.600	12,670
<u>Department of Education</u>		
<i>Department of Education</i>		
Education Consolidation Improvement Act of 1981:		
Title I: Grants to Local Educational Agencies	84.010	437,876
Title I: State Grants for Innovation Programs	84.298	7,954
Title II: Part A, Improving Teacher Quality	84.367	125,417
Title II: Education for Economic Security	84.048	47,140
Elementary and Secondary Education Act (ESEA):		
Special Education – Grants to States	84.027	879,999
Special Education – Preschool Grants	84.173	15,571
Teaching American History Grant	84.251	8,814
Vocational Education:		
Tech Prep Education	84.318	8,510
Adult Education	84.002	61,139
Special Projects:		
Class Size Reduction	84.365	5,064
Safe and Drug Free Schools and Communities	84.186	12,245
<u>Federal Emergency Management Agency</u>		
<i>Department of Emergency Services</i>		
Emergency Management Assistance	83.503	6,741
Hazard Mitigation Grant	97.039	249,706
<u>Election Assistance Commission</u>		
<i>Virginia State Board of Elections</i>		
Help America Vote Act	90.401	9,500
Total Expenditures of Federal Awards		<u>\$ 2,662,898</u>

Note 1: Basis of Accounting

This schedule was prepared on the modified accrual basis of accounting.

Note 2: Nonmonetary Assistance

Nonmonetary assistance is reported in the Schedule of Expenditures of Federal Awards at the fair market value of the food commodities disbursed. At June 30, 2007, the Component Unit – School Division had food commodities in inventory of \$27,367.

**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 Members of the City Council
City of Salem, Virginia
Salem, Virginia

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salem, Virginia as of and for the year ended June 30, 2007, which collectively comprise the City's basic financial statements and have issued our report thereon dated November 15, 2007. We conducted our audit 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 *Specifications for Audits of Counties, Cities, and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions 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 City's internal control.

Our consideration of the 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 the 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 basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, including certain provisions of the compliance matters described in the Summary of Compliance Matters, 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 instances of noncompliance that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as items 07-1, 07-2, and 07-3.**

We noted certain matters that we reported to management of the City in a separate letter dated November 15, 2007.

The City's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the City's response and, accordingly, we express no opinion on it.

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

Brown, Edwards & Company, S. L. P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 15, 2007

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

To the Honorable Members of the City Council
City of Salem, Virginia
Salem, Virginia

Compliance

We have audited the compliance of the City of Salem, Virginia 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, 2007. The City'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'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 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 each of its major federal programs for the year ended June 30, 2007.

Internal Control over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with the 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, 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 more than a 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 more than a 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 solely for the information and use of management, state and federal awarding agencies and pass-through entities, and the School Board. It is not intended to be and should not be used by anyone other than those specified parties.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 15, 2007

CITY OF SALEM, VIRGINIA

SUMMARY OF COMPLIANCE MATTERS

June 30, 2007

As more fully described in the 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*, we performed tests of the City's compliance with certain provisions of the laws, regulations, contracts, and grants shown below.

STATE COMPLIANCE MATTERS

Code of Virginia:

Budget and Appropriation Laws
Cash and Investment Laws
Conflicts of Interest Act
Debt Provisions
Local Retirement Systems
Procurement Laws
Uniform Disposition of Unclaimed Property Act
Sheriff Internal Controls

State Agency Requirements:

Education
Comprehensive Services Act

FEDERAL COMPLIANCE MATTERS

U.S. Office of Management and Budget (OMB A-133) Compliance Supplement:

Provisions and conditions of agreements related to federal programs selected for testing.

CITY OF SALEM, VIRGINIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2007

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an **unqualified opinion** on the basic financial statements.
2. **No significant deficiencies** related to the audit of the financial statements are reported in the 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*.
3. **No instance of noncompliance** material to the basic financial statements was disclosed during the audit.
4. **No significant deficiencies** are disclosed in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with *OMB Circular A-133*.
5. The auditor's report on compliance for the major federal award programs expresses an **unqualified opinion**.
6. The audit disclosed **no audit findings** relating to major programs.
7. The programs tested as major programs include:

National School Lunch Program	10.555
National School Breakfast Program	10.553
Special Education – Grants to States	84.027
Special Education – Preschool Grants	84.173

8. The threshold for distinguishing Types A and B programs was **\$300,000**.
9. The School Board was **determined to be a low-risk auditee**.

B. FINDINGS – FINANCIAL STATEMENT AUDIT

None.

C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAMS

None.

D. FINDINGS AND QUESTIONED COSTS – COMMONWEALTH OF VIRGINIA

07-1: Disclosure Forms – Conflict of Interest Act

Condition:

One individual out of 38 did not file their statement of economic interest by the January 16, 2007 deadline as required by the *Code of Virginia*.

Recommendation:

Steps should be taken to ensure timely and complete filing of the statements of economic interest as required by the *Code of Virginia*.

Management's Response:

The auditee concurs.

CITY OF SALEM, VIRGINIA

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended June 30, 2007**

D. FINDINGS AND QUESTIONED COSTS – COMMONWEALTH OF VIRGINIA (Continued)

07-2: Highway Maintenance Finding

Condition:

The City did not file their June 30, 2006 Highway Finance Survey with the Virginia Department of Transportation by the March 15, 2007 deadline.

Recommendation:

Steps should be taken to ensure timely filing of the Highway Finance Survey with the Virginia Department of Transportation.

Management's Response:

The auditee concurs.

07-3: Unclaimed Property

Condition:

As of June 30, 2007 there were checks noted in the Agency funds as outstanding for more than five years. Checks outstanding more than five years are required to be filed annually on the unclaimed property report to the State Treasurer and remitted to the State agency for disposition.

Recommendation:

Bank reconciliations should be reviewed periodically for checks outstanding more than five years and if in existence, include the checks on the unclaimed property report and remit those checks to the State agency.

Management's Response:

The auditee concurs with this recommendation.

**Department of Finance
City of Salem, Virginia**

Frank P. Turk
Angela A. Sellers

Director of Finance
Assistant Director of Finance

Accounting/Accounts Payable/Purchasing

Vickie L. Akers
Christina M. Brannan
Rowena W. Epperly
Mary Ann Penney, CPA
Susan L. Peterson, CPA
Tammy H. Todd, CPA
Karen M. Vaught
Kathryn B. Williams

Accounting Assistant
Accountant
Buyer
Senior Accountant
Senior Accountant
Accounting Supervisor
Accounting Technician
Accounting Assistant

Administrative

Alyson R. Chaisson

Finance Administrative
Secretary/Accounting Technician

Payroll

Kandis V. Necessary
Patricia K. Poage

Payroll Technician
Payroll Supervisor