

**CITY OF DEFIANCE
DEFIANCE COUNTY, OHIO**

*Basic
Financial Statements*
(Audited)

FOR THE YEAR ENDED
DECEMBER 31, 2004

JOHN SEELE, FINANCE DIRECTOR



**Auditor of State
Betty Montgomery**

Members of Council
City of Defiance
631 Perry Street
Defiance, Ohio 43512

We have reviewed the Independent Auditors' Report of the City of Defiance, Defiance County, prepared by Julian & Grube, Inc. for the audit period January 1, 2004 through December 31, 2004. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The City of Defiance is responsible for compliance with these laws and regulations.

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BETTY MONTGOMERY
Auditor of State

October 21, 2005

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**CITY OF DEFIANCE, OHIO
 BASIC FINANCIAL STATEMENTS
 FOR THE YEAR ENDED DECEMBER 31, 2004**

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JULIAN & GRUBE, INC.

“SERVING OHIO LOCAL GOVERNMENTS”

333 County Line Road West
Westerville, Ohio 43082

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Independent Auditor’s Report

Members of Council and Mayor
City of Defiance
631 Perry Street
Defiance, OH 43082

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Defiance, Defiance County, Ohio, (the “City”), as of and for the year ended December 31, 2004, which collectively comprise the City’s basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City’s management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Defiance, Defiance County, as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the General fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As disclosed in Note 3, the City restated capital assets due to errors and omissions.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 9, 2005, 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 grants 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.

Members of Council and Mayor
City of Defiance
Page Two

The management's discussion and analysis is not a required part of the basic financial statements but is 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 supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in cursive script that reads "Julian & Grube, Inc.".

Julian & Grube, Inc.
September 9, 2005

CITY OF DEFIANCE, OHIO

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEAR ENDED DECEMBER 31, 2004 UNAUDITED

The management's discussion and analysis of the City of Defiance's (the "City") financial performance provides an overall review of the City's financial activities for the year ended December 31, 2004. The intent of this discussion and analysis is to look at the City's financial performance as a whole; readers should also review the basic financial statements and the notes to the basic financial statements to enhance their understanding of the City's financial performance.

Financial Highlights

Key financial highlights for 2004 are as follows:

- The total net assets of the City increased \$2,550,924. Net assets of governmental activities increased \$1,717,946 or 17.41% over 2003 and net assets of business-type activities increased \$832,978 or 5.07% over 2003.
- General revenues accounted for \$8,216,305 of total governmental activities revenue. Program specific revenues accounted for \$2,882,586 or 21.60% of total governmental activities revenue. The City also had an extraordinary item in the reimbursement of insurance claims for \$260,683 and a special item for the sale of land for \$1,983,137.
- The City had \$10,598,452 in expenses related to governmental activities; \$2,882,586 of these expenses was offset by program specific charges for services, grants or contributions. The remaining expenses of the governmental activities of \$7,715,866 were offset by general revenues (primarily property taxes, income taxes and unrestricted grants and entitlements) of \$8,216,305.
- The City has two major funds, the general fund and capital improvements fund. The general fund had revenues of \$7,233,732 in 2004. This represents an increase of \$236,264 from 2003 revenues. The expenditures of the general fund which totaled \$7,707,245 in 2004, increased \$43,078 from 2003. The net increase in fund balance for the general fund was \$557,807 or 40.76%.
- The capital improvements fund had revenues of \$1,537,392 in 2004. This represents an increase of \$158,906 from 2003 revenues. The expenditures of the capital improvements fund, which totaled \$1,824,610 in 2004, increased \$379,008 from 2003. The net decrease in fund balance for the capital improvements fund was \$286,065 or 33.08%.
- Net assets for the business-type activities, which are made up of the Water, Sewer, Refuse and Utility Deposit enterprise funds, increased in 2004 by \$832,978. This increase in net assets was due primarily to adequate charges for services revenue to cover operating expenses.

Using this Annual Financial Report

This annual report consists of a series of financial statements and notes to these statements. These statements are organized so the reader can understand the City as a financial whole, an entire operating entity. The statements then proceed to provide an increasingly detailed look at specific financial activities.

The statement of net assets and statement of activities provide information about the activities of the City as a whole, presenting both an aggregate view of the City's finances and a longer-term view of those finances. Fund financial statements provide the next level of detail. For governmental funds, these statements tell how services were financed in the short-term as well as what remains for future spending. The fund financial statements also look at the City's most significant funds with all other nonmajor funds presented in total in one column.

CITY OF DEFIANCE, OHIO

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED**

Reporting the City as a Whole

Statement of Net Assets and the Statement of Activities

While this document contains a large number of funds used by the City to provide programs and activities, the view of the City as a whole looks at all financial transactions and asks the question, "How did we do financially during 2004?" The statement of net assets and the statement of activities answer this question. These statements include all assets, liabilities, revenues and expenses using the accrual basis of accounting similar to the accounting used by most private-sector companies. This basis of accounting will take into account all of the current year's revenues and expenses regardless of when cash is received or paid.

These two statements report the City's net *assets* and changes in those assets. This change in net assets is important because it tells the reader that, for the City as a whole, the financial position of the City has improved or diminished. The causes of this change may be the result of many factors, some financial, some not. Non-financial factors include the City's property tax base, current property tax laws in Ohio restricting revenue growth, facility conditions, required community programs and other factors.

In the statement of net assets and the statement of activities, the City is divided into two distinct kinds of activities:

Governmental activities - Most of the City's programs and services are reported here including police, fire and rescue, street maintenance, capital improvements and general administration. These services are funded primarily by property and income taxes and intergovernmental revenues including federal and state grants and other shared revenues.

Business-type activities - These services are provided on a charge for goods or services basis to recover all or a significant portion of the expenses of the goods or services provided. The City's water, sewer, refuse and utility deposits operations are reported here.

Reporting the City's Most Significant Funds

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Fund financial reports provide detailed information about the City's major funds. The City uses many funds to account for a multitude of financial transactions. However, these fund financial statements focuses on the City's most significant funds. The analysis of the City's major governmental and proprietary funds begins on page 10.

Governmental Funds

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

CITY OF DEFIANCE, OHIO

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED**

Because the focus of the governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, the readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The City maintains a multitude of individual governmental funds. The City has segregated these funds into major funds and nonmajor funds. The City's major governmental funds are the general fund and Capital Improvements fund. Information for major funds is presented separately in the governmental fund balance sheet and in the governmental statement of revenues, expenditures, and changes in fund balances. Data from the other governmental funds are combined into a single, aggregated presentation. The basic governmental fund financial statements can be found on pages 20-24 of this report.

Proprietary Funds

The City maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its water, sewer, refuse and utility deposits management functions. The City's major enterprise funds are the water and sewer funds. Internal service funds are an accounting device used to accumulate and allocate costs internally among the City's various functions. The basic proprietary fund financial statements can be found on pages 25-28 of this report.

Fiduciary Funds

Fiduciary funds are used to account for resources held for the benefit of parties outside the City. Fiduciary funds are not reflected in the government-wide financial statement because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. Agency funds are the City's only fiduciary fund type. The basic fiduciary fund financial statement can be found on page 29 of this report.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. These notes to the basic financial statements can be found on pages 30-62 of this report.

CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED

Government-Wide Financial Analysis

The table below provides a summary of the City's net assets for 2004 and 2003:

	Net Assets					
	Governmental Activities 2004	Business-type Activities 2004	(Restated)		2004 Total	2003 Total
			Governmental Activities 2003	Business-type Activities 2003		
<u>Assets</u>						
Current and other assets	\$ 10,703,990	\$ 3,797,391	\$ 8,405,427	\$ 4,764,340	\$ 14,501,381	\$ 13,169,767
Capital assets	<u>5,369,843</u>	<u>40,522,108</u>	<u>5,886,911</u>	<u>40,501,532</u>	<u>45,891,951</u>	<u>46,388,443</u>
Total assets	<u>16,073,833</u>	<u>44,319,499</u>	<u>14,292,338</u>	<u>45,265,872</u>	<u>60,393,332</u>	<u>59,558,210</u>
<u>Liabilities</u>						
Long-term liabilities outstanding	2,128,366	25,104,107	2,207,404	26,322,546	27,232,473	28,529,950
Other liabilities	<u>2,360,470</u>	<u>1,951,213</u>	<u>2,217,883</u>	<u>2,512,125</u>	<u>4,311,683</u>	<u>4,730,008</u>
Total liabilities	<u>4,488,836</u>	<u>27,055,320</u>	<u>4,425,287</u>	<u>28,834,671</u>	<u>31,544,156</u>	<u>33,259,958</u>
<u>Net Assets</u>						
Invested in capital assets, net of related debt	2,968,656	14,168,848	3,507,634	12,512,562	17,137,504	16,020,196
Restricted	4,356,637	-	4,273,350	-	4,356,637	4,273,350
Unrestricted	<u>4,259,704</u>	<u>3,095,331</u>	<u>2,086,067</u>	<u>3,918,639</u>	<u>7,355,035</u>	<u>6,004,706</u>
Total net assets	<u>\$ 11,584,997</u>	<u>\$ 17,264,179</u>	<u>\$ 9,867,051</u>	<u>\$ 16,431,201</u>	<u>\$ 28,849,176</u>	<u>\$ 26,298,252</u>

Over time, net assets can serve as a useful indicator of a government's financial position. At December 31, 2004, the City's assets exceeded liabilities by \$28,849,176. At year-end, net assets were \$11,584,997 and \$17,264,179 for the governmental activities and the business-type activities, respectively.

Capital assets reported on the government-wide statements represent the largest portion of the City's net assets. At year-end, capital assets represented 33.41% of total assets. Capital assets include land, buildings and improvements, improvements other than buildings, equipment, vehicles and infrastructure. Capital assets, net of related debt to acquire the assets at December 31, 2004, were \$2,968,656 and \$14,168,848 in the governmental activities and business-type activities, respectively. These capital assets are used to provide services to citizens and are not available for future spending. Although the City's investment in capital assets is reported net of related debt, it should be noted that the resources to repay the debt must be provided from other sources, since capital assets may not be used to liquidate these liabilities.

As of December 31, 2004, the City is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities.

A portion of the City's net assets, \$4,356,637, represents resources that are subject to external restriction on how they may be used. In the governmental activities, the remaining balance of unrestricted net assets of \$4,259,704 may be used to meet the government's ongoing obligations to citizens and creditors.

CITY OF DEFIANCE, OHIO

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED**

The table below shows the changes in net assets for fiscal year 2004.

	Change in Net Assets					
	Governmental	Business-type	Governmental	Business-type	2004	2003
	Activities	Activities	Activities	Activities	Total	Total
	<u>2004</u>	<u>2004</u>	<u>2003</u>	<u>2003</u>		
Revenues						
Program revenues:						
Charges for services	\$ 1,689,230	\$ 7,592,953	\$ 1,656,674	\$ 7,631,409	\$ 9,282,183	\$ 9,288,083
Operating grants and contributions	1,193,356	255,064	1,165,264	-	1,448,420	1,165,264
Capital grants and contributions	-	-	20,871	312,900	-	333,771
Total program revenues	<u>2,882,586</u>	<u>7,848,017</u>	<u>2,842,809</u>	<u>7,944,309</u>	<u>10,730,603</u>	<u>10,787,118</u>
General revenues:						
Property taxes	877,410	-	854,507	-	877,410	854,507
Income taxes	6,052,905	-	5,661,947	-	6,052,905	5,661,947
Unrestricted grants and entitlements	846,451	-	691,903	-	846,451	691,903
Investment earnings	85,767	34,491	74,251	38,817	120,258	113,068
Gain on sale of capital assets	-	-	190,774	-	-	190,774
Miscellaneous	353,772	65,821	439,148	362,350	419,593	801,498
Total general revenues	<u>8,216,305</u>	<u>100,312</u>	<u>7,912,530</u>	<u>401,167</u>	<u>8,316,617</u>	<u>8,313,697</u>
Total revenues	<u>11,098,891</u>	<u>7,948,329</u>	<u>10,755,339</u>	<u>8,345,476</u>	<u>19,047,220</u>	<u>19,100,815</u>
Expenses:						
General government	2,490,843	-	2,379,094	-	2,490,843	2,379,094
Security of persons and property	4,993,929	-	4,743,623	-	4,993,929	4,743,623
Public health and welfare	316,518	-	235,403	-	316,518	235,403
Transportation	1,087,018	-	887,323	-	1,087,018	887,323
Community environment	440,540	-	228,585	-	440,540	228,585
Leisure time activity	1,020,436	-	806,178	-	1,020,436	806,178
Economic development	112,177	-	38,851	-	112,177	38,851
Intergovernmental	6,129	-	5,703	-	6,129	5,703
Other	55,125	-	5,000	-	55,125	5,000
Interest and fiscal charges	75,737	-	72,507	-	75,737	72,507
Water	-	3,486,248	-	3,515,971	3,486,248	3,515,971
Sewer	-	4,112,246	-	3,637,857	4,112,246	3,637,857
Refuse	-	543,170	-	535,534	543,170	535,534
Total expenses	<u>10,598,452</u>	<u>8,141,664</u>	<u>9,402,267</u>	<u>7,689,362</u>	<u>18,740,116</u>	<u>17,091,629</u>
Special item	1,983,137	-	-	-	1,983,137	-
Extraordinary item	260,683	-	-	-	260,683	-
Capital contributions	(1,026,313)	1,026,313	-	-	-	-
Change in net assets	<u>1,717,946</u>	<u>832,978</u>	<u>1,353,072</u>	<u>656,114</u>	<u>2,550,924</u>	<u>2,009,186</u>
Net assets at beginning of year (restated)	<u>9,867,051</u>	<u>16,431,201</u>	<u>8,513,979</u>	<u>15,775,087</u>	<u>26,298,252</u>	<u>24,289,066</u>
Net assets at end of year	<u>\$ 11,584,997</u>	<u>\$ 17,264,179</u>	<u>\$ 9,867,051</u>	<u>\$ 16,431,201</u>	<u>\$ 28,849,176</u>	<u>\$ 26,298,252</u>

CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED

Governmental Activities

Governmental activities net assets increased \$1,717,946 in 2004. This increase is a result of slightly decreasing expenses and an increase in municipal income taxes and a special item from sale of land versus amounts reported in the prior year.

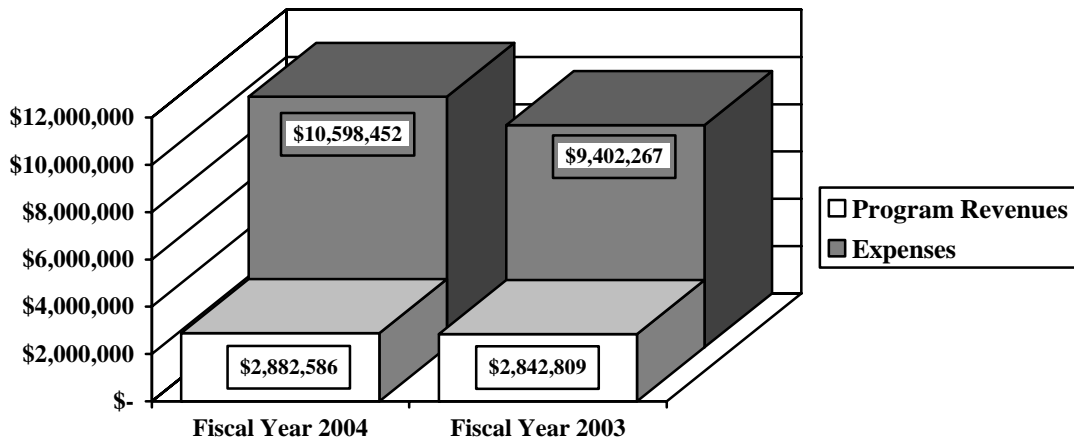
Security of persons and property, which primarily supports the operations of the police and fire departments accounted for \$4,993,929 of the total expenses of the City. These expenses were partially funded by \$927,719 in direct charges to users of the services. Transportation expenses totaled \$1,087,018. Transportation expenses were partially funded by \$509,438 in operating grants and contributions.

The state and federal government contributed to the City a total of \$1,193,356 in operating grants and contributions. These revenues are restricted to a particular program or purpose. Of the total operating grants and contributions, \$603,383 subsidized general government programs.

General revenues totaled \$8,216,305, and amounted to 61.58% of total governmental revenues. These revenues primarily consist of property and income tax revenue of \$6,930,315. The other primary source of general revenues is grants and entitlements not restricted to specific programs, including local government and local government revenue assistance, making up \$846,451. The City had a special item from the sale of land in the amount of \$1,983,137. The City also had an extraordinary item in the reimbursement of insurance claims in the amount of \$260,683.

The statement of activities shows the cost of program services and the charges for services and grants offsetting those services. The following table shows, for governmental activities, the total cost of services and the net cost of services. That is, it identifies the cost of these services supported by tax revenue and unrestricted State grants and entitlements. As can be seen in the graph below, the City is highly dependent upon property and income taxes as well as unrestricted grants and entitlements to support its governmental activities.

Governmental Activities - Program Revenues vs. Total Expenses



CITY OF DEFIANCE, OHIO

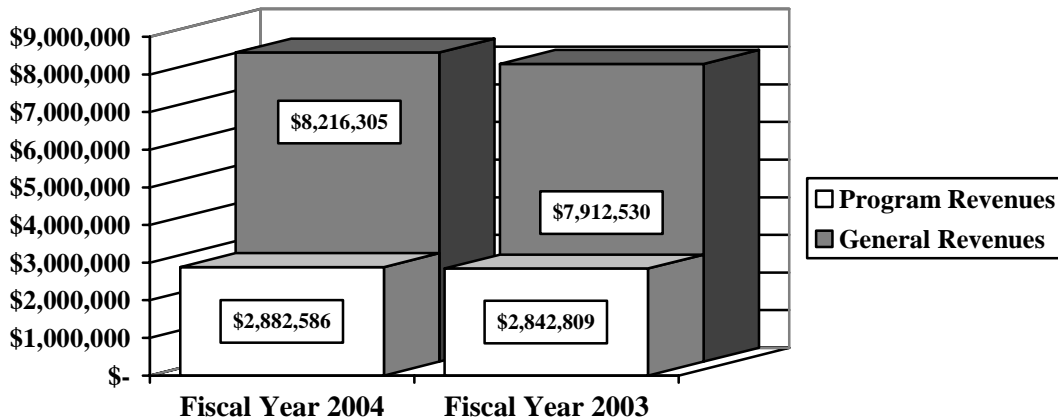
**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED**

Governmental Activities

	Total Cost of Services <u>2004</u>	Net Cost of Services <u>2004</u>	(Restated) Total Cost of Services <u>2003</u>	(Restated) Net Cost of Services <u>2003</u>
Program Expenses:				
General government	\$ 2,490,843	\$ 1,370,894	\$ 2,379,094	\$ 1,538,586
Security of persons and property	4,993,929	3,985,675	4,743,623	3,522,382
Public health and welfare	316,518	247,527	235,403	208,955
Transportation	1,087,018	577,580	887,323	331,395
Community environment	440,540	311,160	228,585	80,096
Leisure time activity	1,020,436	1,003,791	806,178	760,537
Economic development	112,177	82,248	38,851	34,297
Intergovernmental	6,129	6,129	5,703	5,703
Other	55,125	55,125	5,000	5,000
Interest and fiscal charges	<u>75,737</u>	<u>75,737</u>	<u>72,507</u>	<u>72,507</u>
Total	<u>\$ 10,598,452</u>	<u>\$ 7,715,866</u>	<u>\$ 9,402,267</u>	<u>\$ 6,559,458</u>

The dependence upon general revenues for governmental activities is apparent, with 77.52% of expenses supported through taxes and other general revenues.

Governmental Activities - General and Program Revenues

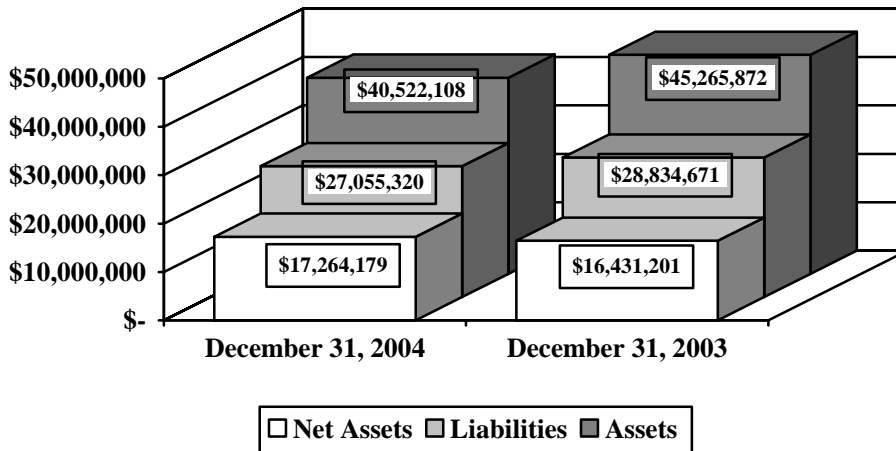


CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED

Business-type Activities

Business-type activities include the water, sewer, refuse and utility deposit enterprise funds. These programs had program revenues of \$7,848,017, general revenues of \$100,312 and expenses of \$8,141,664 for 2004. The graph below shows the business-type activities assets, liabilities and net assets at year-end.

Net Assets in Business - Type Activities



Financial Analysis of the Government's Funds

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

Governmental Funds

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

The schedule below indicates the fund balances and the total change in fund balances as of December 31, 2004 for all major and nonmajor governmental funds.

	Fund Balances 12/31/04	Fund Balances 12/31/03	Increase (Decrease)
Major funds:			
General	\$ 1,926,468	\$ 1,368,661	\$ 557,807
Capital improvements	578,783	864,848	(286,065)
Other nonmajor governmental funds	<u>3,019,463</u>	<u>2,612,141</u>	<u>407,322</u>
Total	<u>\$ 5,524,714</u>	<u>\$ 4,845,650</u>	<u>\$ 679,064</u>

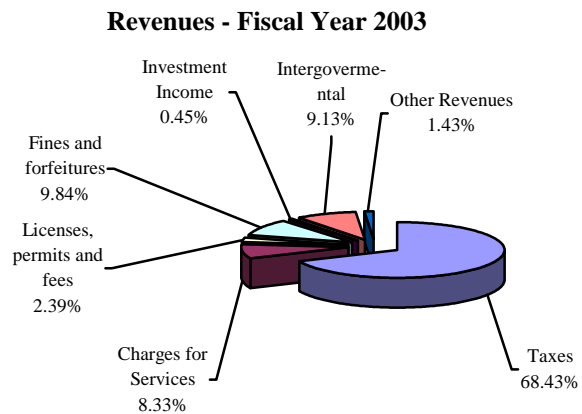
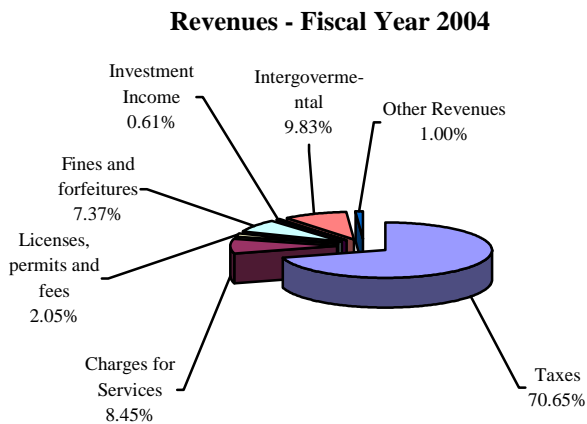
CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED

General Fund

The City's general fund balance increased \$632,284. The table that follows assists in illustrating the revenues of the general fund.

	2004 <u>Amount</u>	2003 <u>Amount</u>	Percentage <u>Change</u>
Revenues			
Income and property taxes	\$ 5,110,717	\$ 4,789,158	6.71 %
Charges for services	613,550	583,127	5.22 %
Licenses, permits and fees	148,319	166,910	(11.14) %
Fines and forfeitures	533,387	688,600	(22.54) %
Investment income	44,196	31,178	41.75 %
Intergovernmental	711,398	638,616	11.40 %
Other	72,165	99,879	(27.75) %
Total	\$ 7,233,732	\$ 6,997,468	3.38 %

Tax revenue represents 70.65% of all general fund revenue. Tax revenue increased slightly by 6.71% from the prior year. The increase in investment income is due to additional investments held by the City during the year. The decrease in fines and forfeitures revenue is due to a decrease in the number of fines the City collected during the year. The increase in intergovernmental revenue is due to an increase of local government and local government revenue assistance to be distributed to local governments during the year compared to 2003. All other revenue remained comparable to 2003.



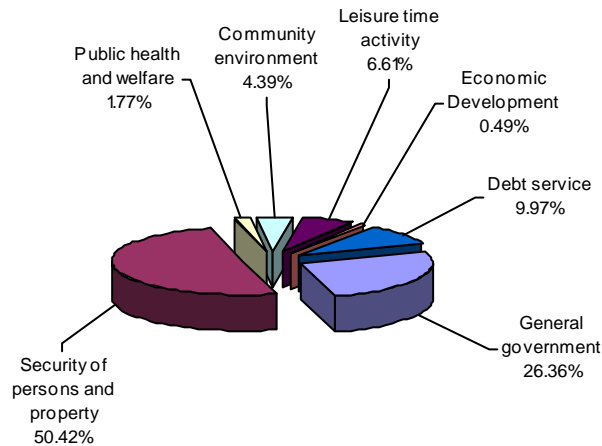
CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED

The table that follows assists in illustrating the expenditures of the general fund.

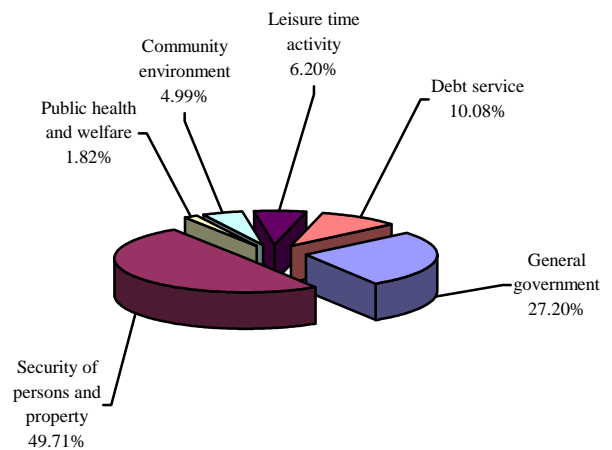
	<u>2004</u> <u>Amount</u>	<u>2003</u> <u>Amount</u>	<u>Percentage</u> <u>Change</u>
<u>Expenditures</u>			
General government	\$ 2,031,496	\$ 2,084,942	(2.56) %
Security of persons and property	3,885,688	3,809,314	2.00 %
Public health and welfare	136,487	139,110	(1.89) %
Community environment	338,152	382,559	(11.61) %
Leisure time activity	509,370	475,334	7.16 %
Economic development	37,392	-	100.00 %
Debt service	768,660	772,908	(0.55) %
Total	<u>\$ 7,707,245</u>	<u>\$ 7,664,167</u>	0.56 %

The most significant decrease was in the area of community environment. This decrease is a large percentage change but is an insignificant amount in comparison to the total expenditures. All other expenditures remained comparable to 2003.

Expenditures - Fiscal Year 2004



Expenditures - Fiscal Year 2003



Capital Improvements Fund

The capital improvements fund had revenues of \$1,537,392 in 2004. This represents an increase of \$158,906 from 2003 revenues. The expenditures of the capital improvements fund, which totaled \$1,824,610 in 2004, increased \$379,008 from 2003. The net decrease in fund balance for the capital improvements fund was \$286,065 or 33.08%.

CITY OF DEFIANCE, OHIO

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2004
UNAUDITED**

Budgeting Highlights

The City's budgeting process is prescribed by the Ohio Revised Code (ORC). Essentially the budget is the City's appropriations which are restricted by the amounts of anticipated revenues certified by the Budget Commission in accordance with the ORC. Therefore, the City's plans or desires cannot be totally reflected in the original budget. If budgeted revenues are adjusted due to actual activity then the appropriations can be adjusted accordingly.

Budgetary information is presented for the general fund. In the general fund, the actual revenues came in \$551,474 higher than they were in the final budget and actual expenditures were \$575,065 lower than the amount in the final budget. These positive variances are the result of the City's conservative budgeting. Budgeted revenues remained consistent from the original to the final budget. Budgeted expenditures increased \$147,765 from the original to the final budget due primarily to an increase in the cost of general government expenditures.

Proprietary Funds

The City's proprietary funds provide the same type of information found in the government-wide financial statements for business-type activities, except in more detail. The only difference between the amounts reported as business-type activities and the amounts reported in the proprietary fund statements are interfund eliminations between proprietary funds and internal balances due to governmental activities for internal service activities. The only interfund activity reported in the government wide statements are those between business-type activities and governmental activities (reported as internal balances and transfers) whereas interfund amounts between various enterprise funds, are reported in the proprietary fund statements.

Capital Assets and Debt Administration

Capital Assets

At the end of fiscal 2004, the City had \$45,891,951 (net of accumulated depreciation) invested in land, buildings and improvements, improvements other than buildings (IOTB), equipment, vehicles, infrastructure and construction in progress. Of this total, \$5,369,843 was reported in governmental activities and \$40,522,108 was reported in business-type activities. The following table shows fiscal 2004 balances compared to 2003:

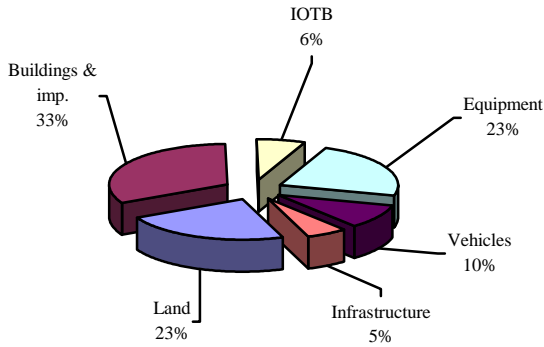
**Capital Assets at December 31
(Net of Depreciation)**

	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Total</u>	
	<u>2004</u>	<u>Restated 2003</u>	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>Restated 2003</u>
Land	\$ 1,243,358	\$ 1,444,719	\$ 267,100	\$ 267,100	\$ 1,510,458	\$ 1,711,819
IOTB	345,666	385,005	432,132	459,844	777,798	844,849
Buildings and improvements	1,730,220	1,848,039	22,415,867	23,101,653	24,146,087	24,949,692
Equipment	1,231,552	1,319,246	241,252	311,086	1,472,804	1,630,332
Vehicles	527,493	593,321	187,706	253,583	715,199	846,904
Infrastructure	291,554	296,581	15,109,197	15,184,363	15,400,751	15,480,944
Construction in progress	-	-	1,868,854	923,903	1,868,854	923,903
Totals	<u>\$ 5,369,843</u>	<u>\$ 5,886,911</u>	<u>\$ 40,522,108</u>	<u>\$ 40,501,532</u>	<u>\$ 45,891,951</u>	<u>\$ 46,388,443</u>

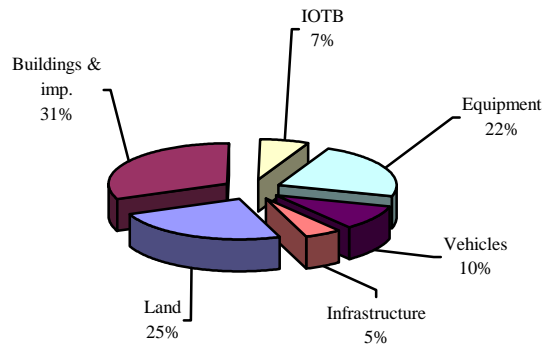
CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004
UNAUDITED

The following graphs show the breakdown of governmental capital assets by category for 2004 and 2003.

Capital Assets - Governmental Activities
2004



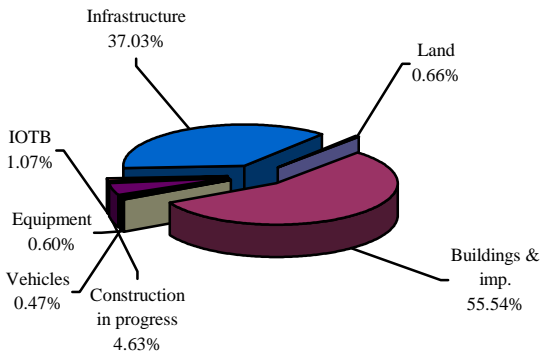
Capital Assets - Governmental Activities
2003



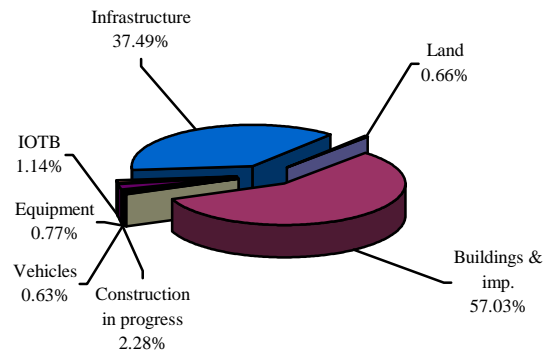
The City added the capital asset category of infrastructure this year. The capital asset category infrastructure includes roads, bridges, culverts, sidewalks and curbs. These items are immovable and of value only to the City, however, the annual cost of purchasing these items is quite significant. The net book value of the City's infrastructure (cost less accumulated depreciation), with only one year reported, represents approximately 5% of the City's total governmental capital assets.

The following graphs show the breakdown of business-type capital assets by category for 2004 and 2003.

Capital Assets - Business-Type Activities
2004



Capital Assets - Business-Type Activities
2003



The City's second largest business-type capital asset category is infrastructure that primarily includes water and sewer lines. These items play a vital role in the income producing ability of the business-type activities. The net book value of the City's infrastructure (cost less accumulated depreciation) represents approximately 37.03% of the City's total business-type capital assets.

See Note 9 for additional analysis of the City's capital assets.

CITY OF DEFIANCE, OHIO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004
UNAUDITED

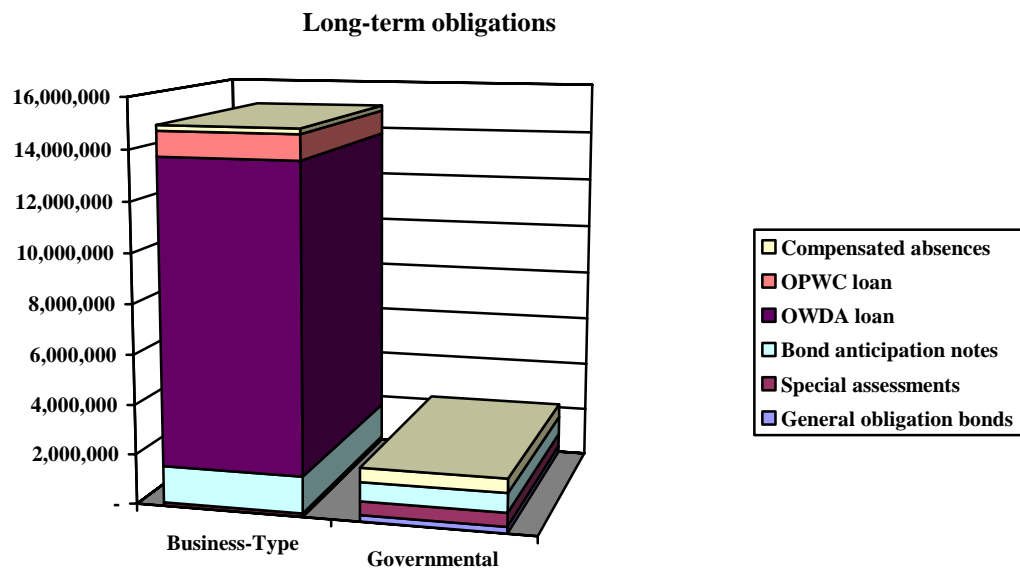
Debt Administration

The City had the following long-term obligations outstanding at December 31, 2004 and 2003:

	Governmental Activities	
	<u>2004</u>	<u>2003</u>
Compensated absences	\$ 562,179	\$ 539,250
General obligation bonds	260,000	290,000
Special assessment bonds	546,187	618,154
Bond anticipation notes	<u>760,000</u>	<u>760,000</u>
Total long-term obligations	<u>\$ 2,128,366</u>	<u>\$ 2,207,404</u>

	Business-type Activities	
	<u>2004</u>	<u>2003</u>
General obligation bonds	\$ 11,625,000	\$ 12,000,000
Special assessment bonds	130,013	134,901
OWDA loan	12,145,142	12,873,756
OPWC loan	988,105	1,056,313
Bond anticipation notes	1,465,000	-
Compensated absences	<u>215,847</u>	<u>257,576</u>
Total long-term obligations	<u>\$ 26,569,107</u>	<u>\$ 26,322,546</u>

A comparison of the long-term obligations by category is depicted in the chart below.



See Note 12 for additional analysis of the City's debt.

CITY OF DEFIANCE, OHIO

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004 UNAUDITED

Economic Conditions and Outlook

Defiance is the commercial and industrial hub of the six-county Northwest Ohio area. It is conveniently located within one-hour drive of Toledo and Fort Wayne. Cleveland, Cincinnati, Detroit and Chicago are all within an easy drive of Defiance. An excellent system of state and U.S. highways serves the transportation needs of the community. Intersecting in Defiance are state routes 18, 15, 66, 281, 424 and 111, and U.S. 24, a major route between Fort Wayne and Toledo.

Ranked for the fourth year in a row in the Top 100 U.S. Small Towns according to 2004 "Site Selection," the City of Defiance has taken a proactive approach to developing new industry. In particular, Enterprise Park on the west side of Defiance offers an excellent site for manufacturing, warehousing, service business or office needs. It consists of 750 acres of flat to gently rolling land which has access to two gas service providers as well as feasibility of two railroads servicing the site. Engineering for Phase I is near completion with a number of industries currently located within the area of Integrity Drive and Precision Way. A detailed plan for future expansion assures that all of the park will be well served by streets and utilities. The City continues to attract interest by introducing new incentives through tax increment financing, enterprise zone agreements, revolving loans and in cooperation with the Defiance County Economic Development Office.

Recently, the Ohio Department of Transportation has committed to providing a connector road from West High Street to Ralston Avenue as part of the U.S. 24 improvements that they anticipate will take place over the next 3 to 5 years. This road will further the development of the existing Olsen Enterprise Park by allowing easier access to U.S. 24. It will also provide access to currently land locked properties owned by the City of Defiance and private enterprise which has already prompted growing interest in the area.

With the activity on the North Side and South Side of U.S. 24 at the State Route 66 interchange, an application has been submitted to the Transportation Review Advisory Council (TRAC) for an 80/20 grant on the widening of this interchange. This project will widen the current lanes from three to five possibly six lanes. Also, it will involve the relocation and widening of ramps for improved access and traffic flow. This project is in conjunction with the improvements on U.S. 24 and represents the City's participation in the ODOT project.

While the City of Defiance is poised for significant positive economic changes, over the past two years the City of Defiance has experienced what many cities across the State of Ohio have experienced. A slowdown in the overall economy decreased funding from the State and Federal levels and a general downsizing in industry have created a poor economic condition for local governments.

Public and private cooperation and support is widespread. Few people do not accept and understand the stark economic conditions that surround local governments in the State of Ohio. For this reason as well as the economic opportunities just around the corner, the City of Defiance will not only survive but will begin to thrive in the coming years.

Contacting the City's Financial Management

This financial report is designed to provide our citizen's, taxpayers, and investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information contact: Mr. John Seele, Finance Director, City of Defiance, 631 Perry Street, Defiance, Ohio 43512.

**BASIC
FINANCIAL STATEMENTS**

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CITY OF DEFIANCE, OHIO

STATEMENT OF NET ASSETS
DECEMBER 31, 2004

	<u>Governmental</u> <u>Activities</u>	<u>Business-type</u> <u>Activities</u>	<u>Total</u>
Assets:			
Equity in pooled cash and cash equivalents.	\$ 3,725,443	\$ 2,951,829	\$ 6,677,272
Investments	291,046	-	291,046
Receivables (net of allowances for uncollectibles):			
Income taxes	1,635,926	-	1,635,926
Property and other local taxes	834,894	-	834,894
Accounts	408,268	300,233	708,501
Loans.	914,776	-	914,776
Special assessments	592,188	239,407	831,595
Due from other governments	2,179,673	1,190	2,180,863
Materials and supplies inventory	43,128	91,579	134,707
Prepayments	94,199	-	94,199
Internal balance.	(15,551)	15,551	-
Restricted assets:			
Equity in pooled cash and cash equivalents	-	197,602	197,602
Capital assets:			
Land and construction-in-progress	1,243,358	2,134,502	3,377,860
Depreciable capital assets, net	4,126,485	38,387,606	42,514,091
Total capital assets.	<u>5,369,843</u>	<u>40,522,108</u>	<u>45,891,951</u>
Total assets.	<u>16,073,833</u>	<u>44,319,499</u>	<u>60,393,332</u>
Liabilities:			
Accounts payable	202,574	88,966	291,540
Accrued wages and benefits	80,792	30,802	111,594
Due to other governments.	329,898	112,476	442,374
Due to claimants.	28,553	-	28,553
Accrued interest payable.	10,996	56,367	67,363
Payable from restricted assets:			
Refunded deposits	-	197,602	197,602
Deferred revenue.	750,000	-	750,000
Claims payable.	122,657	-	122,657
Bond anticipation notes payable.	835,000	1,465,000	2,300,000
Long-term liabilities:			
Due within one year.	1,083,468	1,351,239	2,434,707
Due in more than one year	1,044,898	23,752,868	24,797,766
Total liabilities.	<u>4,488,836</u>	<u>27,055,320</u>	<u>31,544,156</u>
Net assets:			
Invested in capital assets, net of related debt	2,968,656	14,168,848	17,137,504
Restricted for:			
Capital projects	633,866	-	633,866
Debt service.	1,221,999	-	1,221,999
Other purposes	2,500,772	-	2,500,772
Unrestricted	<u>4,259,704</u>	<u>3,095,331</u>	<u>7,355,035</u>
Total net assets	<u>\$ 11,584,997</u>	<u>\$ 17,264,179</u>	<u>\$ 28,849,176</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>Expenses</u>	<u>Program Revenues</u>	
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>
Governmental Activities:			
General government	\$ 2,490,843	\$ 516,566	\$ 603,383
Security of persons and property	4,993,929	927,719	80,535
Public health and welfare	316,518	68,991	-
Transportation.	1,087,018	-	509,438
Community environment	440,540	129,380	-
Leisure time activity	1,020,436	16,645	-
Economic development.	112,177	29,929	-
Intergovernmental	6,129	-	-
Other	53,972	-	-
Interest and fiscal charges.	76,890	-	-
Total governmental activities	<u>10,598,452</u>	<u>1,689,230</u>	<u>1,193,356</u>
Business-type Activities:			
Water	3,486,248	3,586,124	10,510
Sewer	4,112,246	3,413,778	244,554
Other enterprise fund:			
Refuse.	543,170	593,051	-
Total business-type activities	<u>8,141,664</u>	<u>7,592,953</u>	<u>255,064</u>
Total primary government	<u>\$ 18,740,116</u>	<u>\$ 9,282,183</u>	<u>\$ 1,448,420</u>

General Revenues:

Income taxes levied for:	
General purposes	
Special purposes	
Capital purposes	
Property taxes levied for:	
General purposes	
Special purposes	
Grants and entitlements not restricted	
to specific programs	
Investment earnings	
Miscellaneous	
Total general revenues.	

Special Item:

Gain on sale of capital assets	
--	--

Extraordinary Item:

Reimbursement of insurance claims	
---	--

Total general revenues, special item and extraordinary items .

Capital contributions.

Change in net assets.

Net assets at beginning of year (restated).

Net assets at end of year.

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

Net Revenue (Expense) and Changes in Net Assets

Governmental Activities	Business-type Activities	Total
\$ (1,370,894)	\$ -	\$ (1,370,894)
(3,985,675)	-	(3,985,675)
(247,527)	-	(247,527)
(577,580)	-	(577,580)
(311,160)	-	(311,160)
(1,003,791)	-	(1,003,791)
(82,248)	-	(82,248)
(6,129)	-	(6,129)
(53,972)	-	(53,972)
(76,890)	-	(76,890)
<u>(7,715,866)</u>	<u>-</u>	<u>(7,715,866)</u>
-	110,386	110,386
-	(453,914)	(453,914)
-	49,881	49,881
<u>-</u>	<u>(293,647)</u>	<u>(293,647)</u>
<u>(7,715,866)</u>	<u>(293,647)</u>	<u>(8,009,513)</u>
4,634,548	-	4,634,548
21,007	-	21,007
1,397,350	-	1,397,350
560,638	-	560,638
316,772	-	316,772
846,451	-	846,451
85,767	34,491	120,258
353,772	65,821	419,593
<u>8,216,305</u>	<u>100,312</u>	<u>8,316,617</u>
1,983,137	-	1,983,137
<u>260,683</u>	<u>-</u>	<u>260,683</u>
10,460,125	100,312	10,560,437
<u>(1,026,313)</u>	<u>1,026,313</u>	<u>-</u>
1,717,946	832,978	2,550,924
<u>9,867,051</u>	<u>16,431,201</u>	<u>26,298,252</u>
<u>\$ 11,584,997</u>	<u>\$ 17,264,179</u>	<u>\$ 28,849,176</u>

CITY OF DEFIANCE, OHIO

BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2004

	<u>General</u>	<u>Capital Improvements</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets:				
Equity in pooled cash and cash equivalents.	\$ 465,991	\$ 1,120,299	\$ 1,852,177	\$ 3,438,467
Investments	291,046	-	-	291,046
Receivables (net of allowance for uncollectibles):				
Income taxes.	1,252,113	377,521	6,292	1,635,926
Property and other local taxes.	637,406	-	197,488	834,894
Accounts.	112,634	-	276,245	388,879
Loans	-	-	914,776	914,776
Special assessments	-	-	592,188	592,188
Prepayments	94,199	-	-	94,199
Due from other funds.	151,415	-	-	151,415
Due from other governments.	1,840,637	-	339,036	2,179,673
Materials and supplies inventory.	3,000	-	40,128	43,128
	<hr/>	<hr/>	<hr/>	<hr/>
Total assets	<u>\$ 4,848,441</u>	<u>\$ 1,497,820</u>	<u>\$ 4,218,330</u>	<u>\$ 10,564,591</u>
Liabilities:				
Accounts payable.	\$ 129,854	\$ 27,910	\$ 44,810	\$ 202,574
Accrued wages and benefits	70,615	-	10,177	80,792
Due to other funds.	-	-	151,415	151,415
Due to other governments	279,939	-	49,959	329,898
Accrued interest payable	-	1,044	-	1,044
Bond anticipation note payable.	-	835,000	-	835,000
Due to claimants	28,553	-	-	28,553
Deferred revenue.	2,413,012	55,083	942,506	3,410,601
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities	<u>2,921,973</u>	<u>919,037</u>	<u>1,198,867</u>	<u>5,039,877</u>
Fund balances:				
Reserved for encumbrances	212,625	197,707	198,231	608,563
Reserved for materials and supplies inventory.	3,000	-	40,128	43,128
Reserved for prepayments	94,199	-	-	94,199
Reserved for loans	-	-	914,776	914,776
Reserved for debt service	-	-	639,763	639,763
Reserved for noncurrent investments	291,046	-	-	291,046
Unreserved undesignated, reported in:				
General fund	1,325,598	-	-	1,325,598
Special revenue funds.	-	-	1,226,565	1,226,565
Capital projects funds.	-	381,076	-	381,076
	<hr/>	<hr/>	<hr/>	<hr/>
Total fund balances.	<u>1,926,468</u>	<u>578,783</u>	<u>3,019,463</u>	<u>5,524,714</u>
	<hr/>	<hr/>	<hr/>	<hr/>
Total liabilities and fund balances	<u>\$ 4,848,441</u>	<u>\$ 1,497,820</u>	<u>\$ 4,218,330</u>	<u>\$ 10,564,591</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCES
TO NET ASSETS OF GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2004

Total governmental fund balances	\$	5,524,714
<i>Amounts reported for governmental activities on the statement of net assets are different because:</i>		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		5,369,843
Other long-term assets are not available to pay for current period expenditures and therefore are deferred in the funds.		
Income tax	\$ 238,692	
Property and other local taxes	47,406	
Special assessments	592,188	
Intergovernmental	1,782,315	
Total		2,660,601
An internal service fund is used by management to charge the costs of health care to individual funds. The assets and liabilities of the internal service fund is included in governmental activities on the statement of net assets. The net assets of the internal service fund, including an internal balance of \$(15,551), are:		168,157
Accrued interest payable is not due and payable in the current period and therefore is not reported in the funds.		(9,952)
Long-term liabilities, including bonds payable, are not due and payable long-term liabilities are as follows: funds) are as follows:		
General obligation bonds	(260,000)	
Special assessment bonds	(546,187)	
Bond anticipation notes	(760,000)	
Compensated absences	(562,179)	
Total		(2,128,366)
Net assets of governmental activities	\$	11,584,997

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>General</u>	<u>Capital Improvements</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues:				
Income taxes	\$ 4,549,485	\$ 1,371,703	\$ 22,861	\$ 5,944,049
Property and other local taxes	561,232	-	316,772	878,004
Charges for services	613,550	-	29,929	643,479
Licenses, permits and fees	148,319	-	123,144	271,463
Fines and forfeitures	533,387	-	205,207	738,594
Intergovernmental	711,398	146,364	1,253,582	2,111,344
Special assessments	-	-	137,942	137,942
Investment income	44,196	-	39,868	84,064
Other	72,165	19,325	262,282	353,772
Total revenues.	<u>7,233,732</u>	<u>1,537,392</u>	<u>2,391,587</u>	<u>11,162,711</u>
Expenditures:				
Current:				
General government	2,031,496	-	235,192	2,266,688
Security of persons and property.	3,885,688	-	657,597	4,543,285
Public health and welfare	136,487	-	-	136,487
Transportation	-	-	769,930	769,930
Community environment.	338,152	-	-	338,152
Leisure time activity	509,370	-	-	509,370
Economic development and assistance	37,392	-	74,785	112,177
Other	-	-	55,125	55,125
Intergovernmental	-	-	6,129	6,129
Capital outlay.	-	1,812,065	706,628	2,518,693
Debt service:				
Principal retirement	760,000	-	101,967	861,967
Interest and fiscal charges	8,660	12,545	56,289	77,494
Total expenditures	<u>7,707,245</u>	<u>1,824,610</u>	<u>2,663,642</u>	<u>12,195,497</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(473,513)</u>	<u>(287,218)</u>	<u>(272,055)</u>	<u>(1,032,786)</u>
Other financing sources (uses):				
Issuance of notes	760,000	-	-	760,000
Premium on notes	-	1,153	-	1,153
Transfers in	-	-	418,694	418,694
Transfers out	(418,694)	-	-	(418,694)
Sale of capital assets.	690,014	-	-	690,014
Total other financing sources (uses)	<u>1,031,320</u>	<u>1,153</u>	<u>418,694</u>	<u>1,451,167</u>
Extraordinary item:				
Reimbursement of insurance claims.	-	-	260,683	260,683
Net change in fund balances	557,807	(286,065)	407,322	679,064
Fund balances at beginning of year	<u>1,368,661</u>	<u>864,848</u>	<u>2,612,141</u>	<u>4,845,650</u>
Fund balances at end of year	<u>\$ 1,926,468</u>	<u>\$ 578,783</u>	<u>\$ 3,019,463</u>	<u>\$ 5,524,714</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004

Net change in fund balances - total governmental funds	\$	679,064
<i>Amounts reported for governmental activities in the statement of activities are different because:</i>		
Government funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets are allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation expense (\$403,296) exceeded capital outlays (\$93,105) in the current period.		(310,191)
Governmental funds only report the disposal of capital assets to the extent proceeds are received from the sale. In the statement of activities, a gain or loss is reported for each disposal.		(206,877)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.		1,434,477
Proceeds of notes are reported as an other financing source in the governmental funds, but as an increase in liabilities on the statement of net assets.		(760,000)
Repayment of bonds and notes principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities on the statement of net assets.		861,967
In the statement of activities, interest is accrued on outstanding bonds, whereas in governmental funds, an interest expenditure is reported when due.		604
Some expenses reported in the statement of activities, such as compensated absences, do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.		(60,717)
The internal service fund used by management to charge the costs of health care to individual funds is not reported in the statement of activities. Governmental fund expenditures and the related internal service fund revenues are eliminated. The net revenue (expense) of the internal service fund, including the consolidation of internal service fund activity of (\$19,788), is allocated among the governmental activities.		79,619
		<hr style="border-top: 1px solid black;"/>
Change in net assets of governmental activities	\$	<u><u>1,717,946</u></u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
 BUDGET AND ACTUAL (NON-GAAP BUDGETARY BASIS)
 GENERAL FUND
 FOR THE YEAR ENDED DECEMBER 31, 2004

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Income taxes.	\$ 3,917,378	\$ 3,917,378	\$ 4,461,644	\$ 544,266
Property and other local taxes	493,793	493,793	561,232	67,439
Charges for services	545,792	545,792	581,510	35,718
Licenses, permits and fees	156,082	156,082	148,319	(7,763)
Fines and forfeitures	643,709	643,709	548,044	(95,665)
Intergovernmental	627,907	627,907	619,687	(8,220)
Investment income	29,197	29,197	44,189	14,992
Other	58,309	58,309	59,016	707
Total revenues.	<u>6,472,167</u>	<u>6,472,167</u>	<u>7,023,641</u>	<u>551,474</u>
Expenditures:				
Current:				
General government	3,286,961	3,362,082	2,443,347	918,735
Security of persons and property.	4,370,433	4,400,911	4,017,963	382,948
Public health and welfare	142,913	160,625	142,929	17,696
Community environment.	349,998	363,287	350,037	13,250
Leisure time activity	527,624	538,781	527,685	11,096
Economic development and assistance	38,507	38,515	38,515	-
Debt service:				
Principal retirement	-	-	760,000	(760,000)
Interest and fiscal charges	-	-	8,660	(8,660)
Total expenditures	<u>8,716,436</u>	<u>8,864,201</u>	<u>8,289,136</u>	<u>575,065</u>
Deficiency of revenues under expenditures.	<u>(2,244,269)</u>	<u>(2,392,034)</u>	<u>(1,265,495)</u>	<u>1,126,539</u>
Other financing sources (uses):				
Sale of capital assets	-	-	690,014	690,014
Sale of notes	712,714	712,714	760,000	47,286
Transfers out	-	-	(418,694)	(418,694)
Other financing sources.	318,419	318,419	271,459	(46,960)
Total other financing sources (uses)	<u>1,031,133</u>	<u>1,031,133</u>	<u>1,302,779</u>	<u>318,606</u>
Net change in fund balance.	(1,213,136)	(1,360,901)	37,284	1,398,185
Fund balance at beginning of year	402,157	402,157	402,157	-
Prior year encumbrances appropriated	<u>224,404</u>	<u>224,404</u>	<u>224,404</u>	<u>-</u>
Fund balance at end of year.	<u>\$ (586,575)</u>	<u>\$ (734,340)</u>	<u>\$ 663,845</u>	<u>\$ 1,398,185</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

STATEMENT OF NET ASSETS
 PROPRIETARY FUNDS
 DECEMBER 31, 2004

	<u>Business-type Activities - Enterprise Funds</u>				<u>Governmental</u>
	<u>Water</u>	<u>Sewer</u>	<u>Nonmajor</u>	<u>Total</u>	<u>Activities -</u> <u>Internal Service</u> <u>Fund</u>
Assets:					
Current assets:					
Equity in pooled cash and cash equivalents	\$ 1,355,341	\$ 1,305,198	\$ 291,290	\$ 2,951,829	\$ 286,976
Receivables (net of allowance for uncollectibles):					
Accounts	124,984	148,899	26,350	300,233	19,389
Special assessments	100,846	138,561	-	239,407	-
Materials and supplies inventory	86,853	4,726	-	91,579	-
Due from other governments	595	595	-	1,190	-
Total current assets	<u>1,668,619</u>	<u>1,597,979</u>	<u>317,640</u>	<u>3,584,238</u>	<u>306,365</u>
Noncurrent assets:					
Restricted equity in pooled cash and cash equivalents.	-	-	197,602	197,602	-
Capital assets:					
Land and construction-in-progress	1,262,228	872,274	-	2,134,502	-
Depreciable capital assets, net	18,759,804	19,627,802	-	38,387,606	-
Total capital assets	<u>20,022,032</u>	<u>20,500,076</u>	<u>197,602</u>	<u>40,522,108</u>	<u>-</u>
Total noncurrent assets	<u>20,022,032</u>	<u>20,500,076</u>	<u>197,602</u>	<u>40,719,710</u>	<u>-</u>
Total assets	<u>21,690,651</u>	<u>22,098,055</u>	<u>515,242</u>	<u>44,303,948</u>	<u>306,365</u>
Liabilities:					
Current liabilities:					
Accounts payable	66,417	22,549	-	88,966	-
Accrued wages and benefits	17,992	12,810	-	30,802	-
Claims payable	-	-	-	-	122,657
Due to other governments	63,557	48,919	-	112,476	-
Bond anticipation notes payable	-	1,465,000	-	1,465,000	-
General obligations payable - current	410,000	-	-	410,000	-
OPWC loans payable - current	58,800	10,710	-	69,510	-
Special assessment bonds payable - current	-	5,169	-	5,169	-
Accrued interest payable	47,073	9,294	-	56,367	-
OWDA loans payable - current	-	772,816	-	772,816	-
Compensated absences -current	58,116	35,628	-	93,744	-
Total current liabilities	<u>721,955</u>	<u>2,382,895</u>	<u>-</u>	<u>3,104,850</u>	<u>122,657</u>
Current liabilities payable from restricted assets:					
Refundable deposit	-	-	197,602	197,602	-
Noncurrent liabilities:					
Compensated absences	73,546	48,557	-	122,103	-
General obligation bonds payable	11,215,000	-	-	11,215,000	-
Special assessment bonds payable	-	124,844	-	124,844	-
OPWC loans payable	763,306	155,289	-	918,595	-
OWDA loans payable	-	11,372,326	-	11,372,326	-
Total noncurrent liabilities	<u>12,051,852</u>	<u>11,701,016</u>	<u>-</u>	<u>23,752,868</u>	<u>-</u>
Total liabilities	<u>12,773,807</u>	<u>14,083,911</u>	<u>197,602</u>	<u>27,055,320</u>	<u>122,657</u>
Net assets:					
Invested in capital assets, net of related debt	7,574,926	6,593,922	-	14,168,848	-
Unrestricted	1,341,918	1,420,222	317,640	3,079,780	183,708
Total net assets	<u>\$ 8,916,844</u>	<u>\$ 8,014,144</u>	<u>\$ 317,640</u>	<u>17,248,628</u>	<u>\$ 183,708</u>
Adjustment to reflect the consolidation of the internal service fund activity related to enterprise funds				15,551	
Net assets of business-type activities				<u>\$ 17,264,179</u>	

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
 PROPRIETARY FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>Business-type Activities - Enterprise Funds</u>				Governmental
	<u>Water</u>	<u>Sewer</u>	<u>Nonmajor</u>	<u>Total</u>	Activities - Internal Service Fund
Operating revenues:					
Charges for services	\$ 3,528,354	\$ 3,413,778	\$ 593,051	\$ 7,535,183	\$ 1,555,882
Tap-in fees	57,502	-	-	57,502	-
Other	268	-	-	268	-
Total operating revenues	<u>3,586,124</u>	<u>3,413,778</u>	<u>593,051</u>	<u>7,592,953</u>	<u>1,555,882</u>
Operating expenses:					
Personal services	1,433,875	989,604	-	2,423,479	-
Contractual services	10,899	106,967	-	117,866	-
Materials and supplies	508,773	510,054	-	1,018,827	-
Administrative costs	121,456	144,951	-	266,407	-
Utilities expense	241,917	274,439	543,161	1,059,517	-
Claims expense	-	-	-	-	1,497,754
Depreciation	547,214	763,056	-	1,310,270	-
Other	8,145	394	9	8,548	-
Total operating expenses	<u>2,872,279</u>	<u>2,789,465</u>	<u>543,170</u>	<u>6,204,914</u>	<u>1,497,754</u>
Operating income	<u>713,845</u>	<u>624,313</u>	<u>49,881</u>	<u>1,388,039</u>	<u>58,128</u>
Nonoperating revenues (expenses):					
Interest revenue	16,141	18,350	-	34,491	1,703
Interest and fiscal charges	(603,329)	(1,286,229)	-	(1,889,558)	-
Intergovernmental	10,510	244,554	-	255,064	-
Other nonoperating revenue	21,879	43,942	-	65,821	-
Other nonoperating expense	-	(27,404)	-	(27,404)	-
Total nonoperating revenues (expenses)	<u>(554,799)</u>	<u>(1,006,787)</u>	<u>-</u>	<u>(1,561,586)</u>	<u>1,703</u>
Net income (loss) before transfers	159,046	(382,474)	49,881	(173,547)	59,831
Capital Contributions	1,026,313	-	-	1,026,313	-
Changes in net assets	1,185,359	(382,474)	49,881	852,766	59,831
Net assets at beginning of year	<u>7,731,485</u>	<u>8,396,618</u>	<u>267,759</u>		<u>123,877</u>
Net assets at end of year	<u>\$ 8,916,844</u>	<u>\$ 8,014,144</u>	<u>\$ 317,640</u>		<u>\$ 183,708</u>
Adjustment to reflect the consolidation of the internal service fund activity related to enterprise funds				(19,788)	
Change in net assets of business-type activities				<u>\$ 832,978</u>	

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

CITY OF DEFIANCE, OHIO
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>Business-type Activities - Enterprise Funds</u>				Governmental
	<u>Water</u>	<u>Sewer</u>	<u>Nonmajor</u>	<u>Total</u>	Activities - Internal Service Fund
Cash flows from operating activities:					
Cash received from charges for services	\$ 3,412,966	\$ 3,375,549	\$ 608,912	\$ 7,397,427	\$ 1,555,467
Cash received from tap-in fees	57,502	-	-	57,502	-
Cash received from other operations	268	-	-	268	-
Cash payments for personal services	(1,450,664)	(1,038,707)	-	(2,489,371)	-
Cash payments for contractual services	(15,947)	(114,205)	-	(130,152)	-
Cash payments for administrative costs	(121,910)	(161,010)	-	(282,920)	(1,375,097)
Cash payments for materials and supplies	(481,589)	(714,106)	-	(1,195,695)	-
Cash payments for utilities expense	(240,847)	(292,816)	(553,149)	(1,086,812)	-
Cash payments for other expenses	(7,637)	(299)	(9)	(7,945)	-
Net cash provided by operating activities	<u>1,152,142</u>	<u>1,054,406</u>	<u>55,754</u>	<u>2,262,302</u>	<u>180,370</u>
Cash flows from noncapital financing activities:					
Cash received from nonoperating revenues	21,879	43,942	-	65,821	-
Cash payments for nonoperating expenses	-	(27,404)	-	(27,404)	-
Cash received from transfers in	-	-	-	-	-
Cash received from operating grants	<u>11,746</u>	<u>244,546</u>	<u>-</u>	<u>256,292</u>	<u>-</u>
Net cash provided by noncapital financing activities	<u>33,625</u>	<u>261,084</u>	<u>-</u>	<u>294,709</u>	<u>-</u>
Cash flows from capital and related financing activities:					
Cash payments for the acquisition of capital assets	(143,873)	-	-	(143,873)	-
Cash received from issuance of notes	-	1,465,000	-	1,465,000	-
Cash payments for principal retirement	(488,000)	(2,612,710)	-	(3,100,710)	-
Cash payments for interest and fiscal charges	<u>(663,669)</u>	<u>(1,231,450)</u>	<u>-</u>	<u>(1,895,119)</u>	<u>-</u>
Net cash used in capital and related financing activities	<u>(1,295,542)</u>	<u>(2,379,160)</u>	<u>-</u>	<u>(3,674,702)</u>	<u>-</u>
Cash flows from investing activities:					
Cash received from interest earned	<u>16,141</u>	<u>18,350</u>	<u>-</u>	<u>34,491</u>	<u>1,703</u>
Net cash provided by investing activities	<u>16,141</u>	<u>18,350</u>	<u>-</u>	<u>34,491</u>	<u>1,703</u>
Net increase (decrease) in cash and cash equivalents	(93,634)	(1,045,320)	55,754	(1,083,200)	182,073
Cash and cash equivalents at beginning of year	<u>1,448,975</u>	<u>2,350,518</u>	<u>433,138</u>	<u>4,232,631</u>	<u>104,903</u>
Cash and cash equivalents at end of year	<u>\$ 1,355,341</u>	<u>\$ 1,305,198</u>	<u>\$ 488,892</u>	<u>\$ 3,149,431</u>	<u>\$ 286,976</u>

--Continued

CITY OF DEFIANCE, OHIO

STATEMENT OF CASH FLOWS
 PROPRIETARY FUNDS (CONTINUED)
 FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>Business-type Activities - Enterprise Funds</u>				Governmental
	<u>Water</u>	<u>Sewer</u>	<u>Nonmajor</u>	<u>Total</u>	Activities - Internal Service Fund
Reconciliation of operating income to net cash provided by operating activities:					
Operating income.	\$ 713,845	\$ 624,313	\$ 49,881	\$ 1,388,039	\$ 58,128
Adjustments to reconcile operating income to net cash provided by operating activities:					
Depreciation.	547,214	763,056	-	1,310,270	-
Changes in assets and liabilities:					
Increase in accounts receivable	(14,542)	(17,419)	(8,814)	(40,775)	(415)
Increase in special assessments receivable	(100,846)	(20,223)	-	(121,069)	-
(Increase) decrease in materials and supplies inventory	23,838	(159,326)	-	(135,488)	-
Decrease in due from other governments.	-	(595)	-	(595)	-
Decrease in accounts payable	(578)	(33,840)	-	(34,418)	-
Increase (decrease) in contracts payable	-	(52,234)	-	(52,234)	-
Decrease in accrued wages and benefits	(20,072)	(18,121)	-	(38,193)	-
Decrease in compensated absences payable	(6,414)	(35,315)	-	(41,729)	-
Increase in due to other governments	9,697	4,110	-	13,807	-
Increase in utility deposits payable	-	-	14,687	14,687	-
Increase in claims payable.	-	-	-	-	122,657
Total adjustments	<u>438,297</u>	<u>430,093</u>	<u>5,873</u>	<u>874,263</u>	<u>122,242</u>
Net cash provided by operating activities.	<u>\$ 1,152,142</u>	<u>\$ 1,054,406</u>	<u>\$ 55,754</u>	<u>\$ 2,262,302</u>	<u>\$ 180,370</u>

Noncash Item: The City had capital contributions of \$1,026,313 from the Capital Improvement fund to the water fund related to water lines.

CITY OF DEFIANCE, OHIO

**STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUND
DECEMBER 31, 2004**

	<u>Agency</u>
Assets:	
Cash in segregated accounts.	\$ 42,635
Total assets	<u>\$ 42,635</u>
Liabilities:	
Due to other governments.	\$ 42,635
Total liabilities	<u>\$ 42,635</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

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CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 1 - DESCRIPTION OF THE CITY

The City of Defiance, Ohio (the "City"), located in Defiance County, is a politic and corporate body established for the purpose of exercising the rights and privileges conveyed to it by the constitution and laws of the State of Ohio and its charter. The City operates under a Council/Mayor form of government and provides the following services to its residents: public safety, highways and streets, water sanitation, health and social services, culture-recreation, public improvements, planning and zoning, and general administrative services.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements (BFS) of the City have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to local governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial principles. The City also applies Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989, to its governmental and business-type activities and to its proprietary funds provided they do not conflict with or contradict GASB pronouncements. The City has the option to also apply FASB Statements and Interpretations issued after November 30, 1989 to its business-type activities and enterprise funds, subject to this same limitation. The City has elected not to apply these FASB Statements and Interpretations. The most significant of the City's accounting policies are described below.

A. Reporting Entity

For financial reporting purposes, the City's BFS include all funds, agencies, boards, commissions, and departments for which the City is financially accountable. Financial accountability, as defined by the GASB, exists if the City appoints a voting majority of an organization's governing board and is either able to impose its will on that organization or there is a potential for the organization to provide specific financial benefits to, or impose specific burdens on, the City. The City may also be financially accountable for governmental organizations with a separately elected governing board, a governing board appointed by another government, or a jointly appointed board that is fiscally dependent on the City. The City also took into consideration other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's basic financial statements to be misleading or incomplete. Based upon the foregoing criteria, the City has no component units.

The primary government consists of all funds, agencies, departments and offices that are not legally separate from the City. The primary government includes the City departments and agencies that provide the following services: police protection, fire fighting and prevention, emergency medical services, street maintenance and repair, parks and recreation, wastewater, water, public service and planning and zoning.

The following organizations are described due to its relationship with the City.

JOINTLY GOVERNED ORGANIZATIONS

Maumee Valley Planning Organization (MVPO) - The City is a member of MVPO, which is a jointly governed organization between Defiance, Fulton, Henry, Paulding, and Williams Counties and the respective townships and municipalities in each of those counties. The purpose of MVPO is to act as a joint regional planning commission to write and administer Community Development Block Grants (CDBG) and help with housing rehabilitation in the area. In 2004, the City paid \$25,000 to MVPO.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

MVPO is governed by a Board consisting of fifteen members. The Board is made up of one County Commissioner from each member County as well as one township representative and one municipal representative for each of the five member counties. The main sources of revenue are fees charged by MVPO to administer CDBG grants and a per capita amount from each City.

Noble Township - City of Defiance Joint Economic Development District - The City and Noble Township agreed to create a joint economic development district, (the "District"). The District is wholly situated within Noble Township, Defiance County. The purpose of the District is to facilitate economic development to create and preserve employment opportunities within the District.

The District is governed by a board of directors consisting of five members. The board is made up of one representative appointed by the City, Noble Township, the District business owners' association, the District employee's association and one "at-large member". The main source of revenue is a tax levied upon the income earned by persons working in the District and the net profits of businesses located in the District. The tax is at rates equal to those levied upon earned income and profits by the City.

JOINT VENTURES WITHOUT EQUITY INTEREST

Multi-Area Narcotics Task Force (MANTF) - The City is a member of the MANTF, which is a joint venture between Defiance, Paulding and Putnam Counties and the Cities of Defiance and Bryan. The purpose of the drug task force is to act as a joint task force in the fight against narcotics. The MANTF is jointly controlled by the chief law enforcement officer of each respective entity.

The main source of revenue for the MANTF is from federal grants and local matching shares by the entities. The City has no ongoing financial responsibility to the MANTF. The City has indirect access to the net resources of the MANTF since the City is able to influence the MANTF to use its surplus resources to undertake projects of interest to the City's residents. This access to the net resources of the Board has not been explicitly defined, nor is it currently measurable. The City contributed \$7,537 to the MANTF in 2004. Complete financial statements for the MANTF can be obtained through the Defiance City Sheriff's Office located at 113 Biede Street, Defiance, Ohio.

Community Improvement Corporation of Defiance County (Corporation) - The Corporation shall be exercised, conducted, and controlled by the Board of Trustees, which Board shall number a minimum of nine (9) and a maximum of fifteen (15) trustees with forty percent (40%) of the Trustees to be elected officials. Further each shall be a Member of the Corporation and all of whom shall be citizens of the United States. Defiance County, City of Defiance, Village of Hicksville, and Defiance County Townships participate in the operation of the Corporation. The Corporation duties are to advance, encourage and promote the industrial, economic, commercial and civic development.

The Defiance County Economic Development Employment Agreement between the Board of Trustees of the Corporation and the Defiance County Director of Economic Development states that the county's Director of Economic Development may serve as executive director of the Corporation, such corporation having agreed to furnish the county with the funds needed to pay his salary. The City of Defiance partially funds the Corporation to pay the salary of the Director of the Defiance County Economic Development. The City made \$35,000 in payments to the Corporation in 2004. The City's degree of control over the Board is limited to its representation on the Board.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

RELATED ORGANIZATION

Defiance Public Library - The Defiance Public Library is a distinct political subdivision of the State of Ohio created under Chapter 3375 of the Ohio Revised Code. The Library is governed by a Board of Trustees appointed by City Council. The Board of Trustees possesses its own contracting and budgeting authority, hires and fires personnel, and does not depend on the District for operational subsidies. Although the City does serve as the taxing authority and may issue tax related debt on behalf of the Library, its role is limited to a ministerial function. The determination to request approval of a tax, the rate and the purpose are discretionary decisions made solely by the Board of Trustees. Financial information can be obtained from the Defiance Public Library, Mary Kay Reineke, Clerk/Treasurer, at 320 Fort Street, Defiance, Ohio 43512

B. Basis of Presentation - Fund Accounting

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

Government-wide Financial Statements - The statement of net assets and the statement of activities display information about the City as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The activities of the internal service fund is eliminated to avoid "doubling up" revenues and expenses. The statements distinguish between those activities of the City that are governmental and those that are considered business-type activities.

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

Fund Financial Statements - During the year, the City segregates transactions related to certain City functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the City at this more detailed level. The focus of governmental and enterprise fund financial statements is on major funds. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. The internal service fund is presented in a single column on the face of the proprietary fund financial statements. Fiduciary funds are reported by type.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

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 operation. The principal operating revenues of the City's proprietary funds are charges for services. Operating expenses from the enterprise funds include personnel and other expenses related to sewer, water, refuse, and utility deposits and operating expenses for the internal service fund include claims and administrative expenses. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

The agency funds do not report a measurement focus as they do not report operations.

C. Fund Accounting

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

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

General Fund - The general fund accounts for all financial resources except those required to be accounted for in another fund.

Capital Improvements Fund - The capital improvements fund accounts for resources used to purchase equipment and construct capital assets.

Other governmental funds of the City are used to account for (a) the accumulation of resources for, and payment of, general long-term debt principal, interest and related costs; (b) financial resources to be used for the acquisition, construction, or improvement of capital facilities other than those financed by proprietary funds; and (c) for grants and other resources whose use is restricted to a particular purpose.

Proprietary Funds - Proprietary fund reporting focuses on changes in net assets, financial position and cash flows. Proprietary funds are classified as either enterprise or internal service.

Enterprise Funds - The enterprise funds may be used to account for any activity for which a fee is charged to external users for goods or services. The following are the City's major enterprise funds:

Water Fund - This fund accounts for the provision of water treatment and distribution to its residential and commercial users located within the City.

Sewer Fund - This fund accounts for the provision of sanitary sewer service to the residents and commercial users located within the City.

Other enterprise funds of the City are used to account for refuse collection and utility deposits. These funds are nonmajor funds whose activity has been aggregated and presented in a single column in the BFS.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

Internal Service Fund - The internal service fund accounts for the financing of services provided by one department or agency to other departments or agencies of the City on a cost-reimbursement basis. The City's internal service fund is used to account for employee health insurance.

Fiduciary Funds - Fiduciary fund reporting focuses on net assets and changes in net assets. The fiduciary fund category is split into four classifications: pension trust funds, investment trust funds, private-purpose trust funds and agency funds. Trust funds are used to account for assets held by the City under a trust agreement for individuals, private organizations, or other governments and are therefore not available to support the City's own programs. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The City's only fiduciary funds are agency funds.

D. Measurement Focus and Basis of Accounting

Government-wide Financial Statements - The government-wide financial statements are prepared using the economic resources measurement focus. All assets and all liabilities associated with the operation of the City are included on the statement of net assets.

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

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

E. Basis of Accounting

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

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

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

Nonexchange transactions, in which the City receives value without directly giving equal value in return, include income taxes, property taxes, grants, entitlements and donations. On an accrual basis, revenue from income taxes is recognized in the period in which the income is earned (See Note 7). Revenue from property taxes is recognized in the year for which the taxes are levied (See Note 6). Revenue from grants, entitlements and donations is recognized in the year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the year when use is first permitted, matching requirements, in which the City must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the City on a reimbursement basis. On a modified accrual basis, revenue from nonexchange transactions must also be available before it can be recognized.

Under the modified accrual basis, the following revenue sources are considered to be both measurable and available at year-end: income tax, state-levied locally shared taxes (including gasoline tax, local government funds and permissive tax), fines and forfeitures, fees and special assessments.

Deferred Revenue - Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied.

Property taxes for which there is an enforceable legal claim as of December 31, 2004, but which were levied to finance year 2005 operations, have been recorded as deferred revenue. Special assessments not received within the available period and grants and entitlements received before the eligibility requirements are met are also recorded as deferred revenue.

On governmental fund financial statements, receivables that will not be collected within the available period have also been reported as deferred revenue.

Expenses/Expenditures - On the accrual basis of accounting, expenses are recognized at the time they are incurred.

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

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

F. Budgetary Data

The budgetary process is prescribed by provisions of the Ohio Revised Code and entails the preparation of budgetary documents within an established timetable. The major documents prepared are the tax budget, the certificate of estimated resources and the appropriations resolution, all of which are prepared on the budgetary basis of accounting. The certificate of estimated resources and the appropriations ordinance are subject to amendment throughout the year with the legal restriction that appropriations cannot exceed estimated resources, as certified. The legal level of budgetary control is at the fund, department and object level. Budgetary modifications may only be made by resolution of the City Council at the legal level of control.

Tax Budget - During the first Council meeting in July, the Mayor presents the following fiscal year's annual operating budget to City Council for consideration and passage. The adopted budget is submitted to the County Auditor, as Secretary of the County Budget Commission, by July 20 of each year, for the period January 1 to December 31 of the following year.

Estimated Resources - The County Budget Commission determines if the budget substantiates a need to levy all or part of previously authorized taxes and reviews estimated revenue. The Commission certifies its actions to the City by September 1. As part of this certification, the City receives the official certificate of estimated resources, which states the projected revenue of each fund. Prior to December 31, the City must revise its budget so that the total contemplated expenditures from any fund during the ensuing fiscal year will not exceed the amount available as stated in the certificate of estimated resources. The revised budget then serves as the basis for the annual appropriations measure. On or about January 1, the certificate of estimated resources is amended to include encumbered cash balances at December 31 of the preceding year. The certificate may be further amended during the year if the Finance Director determines, and the Budget Commission agrees, that an estimates need to be either increased or decreased. The amounts reported on the budgetary statement reflect the amounts in the final amended official certificate of estimated resources issued during 2004.

Appropriations - A temporary appropriation ordinance to control expenditures may be passed on or about January 1 of each year for the period January 1 to March 31. An annual appropriation ordinance must be passed by April 1 of each year for the period January 1 to December 31. The appropriation ordinance fixes spending authority at the fund, department and object level. The appropriation ordinance may be amended during the year as new information becomes available, provided that total fund appropriations do not exceed current estimated resources, as certified. The appropriations for a fund may only be modified during the year by an ordinance of Council. The amounts on the budgetary statement reflect the final appropriation amounts, including all amendments and modifications legally enacted by Council.

Lapsing of Appropriations - At the close of each year, the unencumbered balance of each appropriation reverts to the respective fund from which it was appropriated and becomes subject to future appropriations. Encumbrances are carried forward and are not reappropriated as part of the subsequent year appropriations.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

G. Health Care

The Comprehensive Omnibus Budget Reconciliation Act (COBRA) of 1986 required the City to offer and provide terminated or retired employees continued participation in the City’s employee health care benefits program, provided that the employees pay the rate established by the plan administrator. The City incurred no expenditures or revenues in providing these services. The participating former employees make premium payments directly to the City’s Insurance Provider and the Provider is responsible for all claims.

H. Cash and Investments

To improve cash management, cash received by the City other than cash in segregated accounts is pooled. Monies for all funds, including proprietary funds, are maintained in this pool. Individual fund integrity is maintained through the City’s records. Each fund’s interest in the pool is presented as “Equity in Pooled Cash and Cash Equivalents” and “Investment” on the combined balance sheet.

During fiscal year 2004, investments were limited to the State Treasury Asset Reserve of Ohio (STAR Ohio), mutual funds, and the City’s own bonds. Except for nonparticipating investment contracts, investments are reported at fair value which is based on quoted market prices. Nonparticipating investment contracts are reported at cost.

The City has invested funds in STAR Ohio during fiscal year 2004. STAR Ohio is an investment pool managed by the State Treasurer’s Office which allows governments within the state to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio’s share price which is the price the investment could be sold for on December 31, 2004.

Following Ohio statutes, the Council has, by resolution, specified the funds to receive an allocation of interest earnings. The following funds were credited with more interest revenue than would have been received based upon their share of the City’s cash fund balance during 2004:

	<u>Interest Actually Received</u>	<u>Interest Based Upon Share of Cash Fund Balance</u>	<u>Interest Assigned by Other Funds</u>
General Fund	\$ 44,196	\$ 8,521	\$ 35,675
<u>Nonmajor Governmental Funds</u>			
State Highway Improvement Fund	845	555	290
Street Construction, Maintenance, and Repair Fund	546	158	388
Cable TV Contract Fund	845	231	614
Termination Benefits Fund	845	348	497
<u>Enterprise Fund</u>			
Water	16,141	15,568	573

The City has segregated bank accounts for monies held separate from the City’s central bank account. These interest bearing depository accounts are presented on the combined balance sheet as “Cash with Fiscal and Escrow Agents” since they are not required to be deposited into the City treasury.

CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

For purposes of the combined statement of cash flows and for presentation on the combined balance sheet, investments of the cash management pool and investments with original maturities of three months or less at the time they are purchased by the City are considered to be cash equivalents. Investments with an initial maturity of more than three months are reported as investments.

An analysis of the City's investment account at year-end is provided in Note 4.

I. Restricted Assets

Customer deposits are classified as restricted assets because these funds are being held for specified purposes.

J. Inventories of Materials and Supplies

On government-wide and fund financial statements, inventories are presented at the lower of cost or market on a first-in, first-out basis and are expensed when used. Inventories are accounted for using the consumption method.

On the fund financial statements, reported material and supplies inventory is equally offset by a fund balance reserve in the governmental funds which indicates that it does not constitute available spendable resources even though it is a component of net current assets.

Inventory consists of expendable supplies held for consumption.

K. Capital Assets

Governmental capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported both in the business-type activities column of the government-wide statement of net assets and in the respective funds.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated capital assets are recorded at their fair market values as of the date received. The City maintains a capitalization threshold at \$2,500. The City's infrastructure consists of roads, bridges, culverts, and sanitary sewers. Improvements are capitalized; the costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized. Interest incurred during the construction of capital assets is also capitalized.

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

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

<u>Description</u>	<u>Governmental Activities Estimated Lives</u>	<u>Business-type Activities Estimated Lives</u>
Improvements other than buildings	15 - 30 years	N/A
Land improvements	N/A	15 - 30 years
Buildings and improvements	15 - 45 years	30 - 50 years
Furniture and equipment	10 - 30 years	10 - 30 years
Infrastructure	30 years	50 years
Vehicles	6 - 15 years	6 - 15 years

Interest is capitalized on proprietary fund assets acquired with tax-exempt debt. The City’s policy is to capitalize net interest on construction projects until substantial completion of the project. The amount of capitalized interest equals the difference between the interest cost associated with the tax-exempt borrowing used to finance the project from the date of borrowing until completion of the project and the interest earned from temporary investment of the debt proceeds over the same period.

Capitalized interest is amortized on the straight-line method over the estimated useful life of the asset. For 2004, the net interest expense incurred on proprietary fund construction projects was not material.

L. Compensated Absences

Compensated absences of the City consist of vacation leave and sick leave to the extent that payment to the employee for these absences are attributable to services already rendered and are not contingent on a specific event that is outside the control of the City and the employee.

In conformity with GASB Statement No. 16, “Accounting for Compensated Absences”, vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the City will compensate the employees for the benefits through paid time off or some other means. Sick leave benefits are accrued as a liability using the vesting method. The liability is based on the sick leave accumulated at December 31 by those employees who are currently eligible to receive termination payments and by those employees for whom it is probable they will become eligible to receive termination benefits in the future.

American Federation of State, County and Municipal Employees (AFSCME) and non-bargaining employees with a minimum of ten years of service are paid one day for every two days sick leave for the first 120 days of accumulated sick time and one day for every seven days for accumulated sick time in excess of 120 days upon retirement. International Union of Police Associations (IUPA) bargaining unit individuals employed for ten years or more as of December 31, 1991, shall be eligible for sick leave conversion upon retirement at one day for each two days accumulation without limit. Beginning January 1, 1992, an IUPA bargaining unit individual with twenty-two or more years of service, who resigns shall be eligible for payment for one day’s pay for every two days of accumulated but unused sick leave, not to exceed 120 days. International Association of Firefighters (IAFF) bargaining unit individuals with ten or more years of service, shall upon retirement under provision of the Police & Firefighters Pension Fund be eligible for payment of one-half of the employee’s accrued, but unused sick leave earned up to a maximum payment for 50 twenty-four hour days. An IAFF bargaining unit individual with twenty-two or more years of service, who retires or resigned from the City shall be eligible for payment for one-half of accrued, but unused sick leave up to a maximum payment for 50 twenty-four hour days.

CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

The total liability for vacation and sick leave payments has been calculated using pay rates in effect at the balance sheet date, and reduced to the maximum payment allowed by labor contract and/or statute, plus applicable additional salary related payments. City employees are granted vacation and sick leave in varying amounts. In the event of termination, an employee is reimbursed for accumulated vacation and sick leave at various rates.

The entire compensated absence liability is reported on the government-wide financial statements.

On governmental fund financial statements, compensated absences are recognized as liabilities and expenditures to the extent payments come due each period upon the occurrence of employee resignations and retirements. These amounts are recorded in the account "compensated absences payable" in the fund from which the employees who have accumulated leave are paid. The noncurrent portion of the liability is not reported. For proprietary funds, the entire amount of compensated absences is reported as a fund liability.

M. Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities and long-term obligations are reported in the government-wide financial statements, and all payables, accrued liabilities and long-term obligations payable from proprietary funds are reported on the proprietary fund financial statements.

In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current financial resources, are reported as obligations of the funds. However, claims and judgments, compensated absences, and contractually required pension contributions that will be paid from governmental funds are reported as a liability in the fund financial statements only to the extent that they are due for payment during the current year.

N. Prepayments

Payments made to vendors for services that will benefit periods beyond December 31, 2004, are recorded as prepaid items using the consumption method by recording a current asset for the prepaid amount and reflecting the expenditure/expense in the year in which services are consumed.

O. Interfund Balances

On fund financial statements, receivables and payables resulting from short-term interfund loans are classified as "interfund receivables/payables." These amounts are eliminated in the governmental and business-type activities columns of the statement of net assets, except for any net residual amounts due between governmental and business-type activities, which are presented as internal balances.

P. Interfund Activity

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

CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

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

Q. Fund Balance Reserves

Reserved fund balances indicate that portion of fund equity which is not available for current appropriation or use. The unreserved portions of fund equity reflected in the governmental funds are available for use within the specific purposes of the funds.

The City reports a reservation of fund balance for amounts representing encumbrances outstanding, materials and supplies inventory, prepayments, loans, debt service, and noncurrent investments in the governmental fund financial statements.

R. Estimates

The preparation of the BFS in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the BFS and accompanying notes. Actual results may differ from those estimates.

S. Contributions of Capital

Contributions of capital in proprietary fund financial statements arise from outside contributions of capital assets, tap-in fees to the extent they exceed the cost of the connection to the system, or from grants or outside contributions of resources restricted to capital acquisition and construction. Capital contributions are reported as revenue in the proprietary fund financial statements.

T. Net Assets

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

The City applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

U. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the City, these revenues are charges for services for sewer, water, refuse and utility deposits programs. Operating expenses are necessary costs incurred to provide the good or service that is the primary activity of the fund.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

V. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of City Administration and that are either unusual in nature or infrequent in occurrence. During fiscal year 2004, the City incurred a transaction that would be classified as an extraordinary item. The City received \$260,683 in proceeds of reimbursement of insurance claims related to fire damage that occurred to a City building. During fiscal year 2004, the City sold land to Defiance County. The City received \$690,014 in revenue for 2004 and will receive \$750,000 in both 2005 and 2006. This transaction is classified as a special item.

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE

A. Governmental Activities - Restatement of Net Assets

Net assets of the governmental activities have been restated due to errors and omissions in the capital asset balances. This prior period adjustment had the following effect on net assets as previously reported.

	Governmental Activities
Net assets January 1, 2004	\$ 9,665,690
Capital asset adjustment	201,361
Restated governmental activities net assets, January 1, 2004	\$ 9,867,051

B. Deficit Fund Balances

	Deficit
<u>Nonmajor Governmental Funds</u>	
Permissive Tax	\$ 151,740
Fire Pension	178

The general fund is liable for any deficits in these funds and provides transfers when cash is required, not when accruals occur. The deficit fund balances result from adjustments for accrued liabilities. The Permissive Tax special revenue fund did not comply with State law which does not allow for a negative cash balance at year-end.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE - (Continued)

C. Compliance

We noted the following funds which had appropriations in excess of estimated resources contrary to Ohio Revised Code Section 5705.39:

<u>Major/Non-Major Funds</u>	<u>Appropriations</u>	<u>Estimated Resources</u>	<u>Excess</u>
General Fund (Major)	\$8,716,436	\$8,129,861	\$586,575

It was noted that the following funds had appropriations which exceeded estimated resource at December 31, 2004:

<u>Major/Non-Major Funds</u>	<u>Appropriations</u>	<u>Estimated Resources</u>	<u>Excess</u>
General Fund (Major)	\$8,864,201	\$8,129,861	\$734,340
Street Construction, Maintenance and Repair (Non-Major)	847,842	534,432	288,798
Special Projects Fund (Non-Major)	80,000	0	80,000
Cable TV Contract Fee Fund (Non-Major)	24,400	18,743	5,657
Housing Rehabilitation (Non-Major)	375,000	57,457	317,543
Sewer Fund (Major)	7,679,805	6,880,128	799,677
Water Fund (Major)	4,427,854	3,808,789	619,065
Tax Reduction (Non-Major)	32,200	0	32,300
Police Pension (Non-Major)	285,600	259,479	26,121
Fire Damage Repair (Non-Major)	34,000	29,100	4,900

We noted the following funds had expenditures exceeding appropriations contrary to Ohio Revised Code Section 5705.41(B):

	<u>Appropriations</u>	<u>Expenditures</u>	<u>Excess</u>
<u>Major Fund</u>			
General			
City Administrator			
Operating	\$ 48,283	\$ 88,821	\$ 40,538
Finance			
Debt Service	-	768,660	768,660
Law			
Salaries and Wages	162,432	165,882	3,450
Employee Benefits	39,284	40,904	1,620
Fire			
Employee Benefits	219,331	223,701	4,370
Engineering			
Salaries and Wages	92,478	97,311	4,833
Employee Benefits	31,699	33,199	1,500
Capital Improvement			
Capital Outlay	2,724,952	2,843,213	118,261

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE - (Continued)

We noted the Permissive Tax special revenue fund had a negative cash balance at December 31, 2004 contrary to Ohio Revised Code Section 5705.10

NOTE 4 - EQUITY IN POOLED CASH AND CASH EQUIVALENTS

Moneys held by the City are classified by state statute into two categories. Active moneys are public moneys determined to be necessary to meet current demand upon the City treasury. Active moneys must be maintained either as cash in the City treasury, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

Protection of the City's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the treasurer by the financial institution or by a single collateral pool established by the financial institution to secure the repayment of all public moneys deposited with the institution.

Moneys held by the City which are not considered active are classified as inactive. Inactive moneys may be deposited or invested in the following securities:

1. United States Treasury Notes, Bills, Bonds, or any other obligation or security issued by the United States Treasury or any other obligation guaranteed as to principal or interest by the United States;
2. Bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality, including but not limited to, the Federal National Mortgage Association, Federal Home Loan Bank, Federal Farm Credit Bank, Federal Home Loan Mortgage Corporation, Government National Mortgage Association, and Student Loan Marketing Association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
3. Written repurchase agreements in the securities listed above provided that the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least two percent and be marked to market daily, and that the term of the agreement must not exceed thirty days;
4. Bonds and other obligations of the State of Ohio;
5. No-load money market mutual funds consisting exclusively of obligations described in division (1) or (2) and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions;
6. The State Treasurer's investment pool (STAR Ohio);
7. High grade commercial paper for a period not to exceed 180 days in an amount not to exceed twenty-five percent of the City's interim monies available for investment; and
8. Bankers acceptances for a period not to exceed 180 days and in an amount not to exceed twenty-five percent of the City's interim monies available for investment.

The City may also invest any monies not required to be used for a period of six months or more in the following:

1. Bonds of the State of Ohio;

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 4 - EQUITY IN POOLED CASH AND CASH EQUIVALENTS - (Continued)

2. Bonds of any municipal corporation, village, county, township, or other political subdivision of this state, as to which there is no default of principal, interest or coupons; and
3. Obligations of the City.

Investments in stripped principal or interest obligations, reverse repurchase agreements, and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage, and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the City, and must be purchased with the expectation that it will be held to maturity. Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the treasurer or qualified trustee or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

The following information classifies deposits and investments by categories of risk as defined in GASB Statement No. 3, “Deposits With Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements”.

Cash on Hand: At year-end, the City had \$2,250 in undeposited cash on hand which is included on the financial statements of the City as part of “Equity in Pooled Cash and Cash Equivalents.”

Deposits: At year-end, the carrying amount of the City’s deposits was \$896,569 and the bank balance was \$3,959,134. Of the bank balance:

1. \$405,576 was covered by federal depository insurance; and
2. \$3,553,558 was uninsured and uncollateralized as defined by GASB even though it was covered by collateral held by third party trustees pursuant to Section 135.81, Ohio Revised Code, in single institution collateral pools securing all public funds on deposit with specific depository institutions. Although all state statutory requirements for the deposit of money had been followed, non-compliance with federal requirements could potentially subject the City to a successful claim by the FDIC.

Investments: The City’s investments are required to be categorized to give an indication of the level of risk assumed by the City at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the City or its agent in the City’s name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty’s trust department or agent in the City’s name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent, but not in the City’s name. STAR Ohio (an investment pool operated by the Ohio State Treasurer) is an unclassified investment since they are not evidenced by securities that exist in physical or book entry form.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 4 - EQUITY IN POOLED CASH AND CASH EQUIVALENTS - (Continued)

The following is a listing of investments, by category, as of December 31, 2004:

	<u>Category 1</u>	<u>Uncategorized</u>	<u>Reported Amount</u>	<u>Fair Value</u>
Money Market Mutal Funds	\$ -	\$ 2,912,561	\$ 2,912,561	\$2,912,561
City of Defiance bonds	291,046	-	291,046	291,046
Investment in STAR Ohio	<u>-</u>	<u>3,106,129</u>	<u>3,106,129</u>	<u>3,106,129</u>
 Total investments	 <u>\$ 291,046</u>	 <u>\$ 6,018,690</u>	 <u>\$ 6,309,736</u>	 <u>\$6,309,736</u>

The classification of cash and cash equivalents on the basic financial statements is based on criteria set forth in GASB Statement No. 9, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting".

A reconciliation between the classifications of cash and cash equivalents and investments on the basic financial statements (per GASB Statement No. 9) and the classifications of deposits and investments presented above per GASB Statement No. 3 is as follows:

	<u>Cash and Cash Equivalents/ Deposits</u>	<u>Investments</u>
GASB Statement No. 9	\$ 6,917,509	\$ 291,046
Cash on hand	(2,250)	-
Investments of the cash management pool:		
Investment in STAR Ohio	(3,106,129)	3,106,129
Mutual Funds	<u>(2,912,561)</u>	<u>2,912,561</u>
 GASB Statement No. 3	 <u>\$ 896,569</u>	 <u>\$ 6,309,736</u>

NOTE 5 - INTERFUND TRANSFERS

A. Interfund transfers for the year ended December 31, 2004, consisted of the following, as reported in the fund statements:

Transfers to nonmajor governmental funds from:	
General fund	\$ 418,694
Transfers to Water fund from:	
Capital Improvements fund	<u>1,026,313</u>
Total	<u>\$ 1,445,007</u>

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 5 - INTERFUND TRANSFERS - (Continued)

B. At December 31, 2004, the Permissive Tax special revenue fund has a negative cash balance. This fund overdraft of the internal investment pool has been reported as a fund liability.

Due to general fund from:	
Nonmajor governmental funds	<u>\$ 151,415</u>
Total	<u><u>\$ 151,415</u></u>

NOTE 6 - PROPERTY TAXES

Property taxes include amounts levied against all real, public utility and tangible personal property located in the City. Taxes collected from real property taxes (other than public utility) in one calendar year are levied in the preceding calendar year on the assessed value as of January 1 of that preceding year, the lien date. Assessed values are established by the County Auditor at 35 percent of appraised market value. All property is required to be revaluated every six years. The last revaluation was completed in 1999. Real property taxes are payable annually or semi-annually. The first payment is due January 20, with the remainder payable by July 20.

Taxes collected on tangible personal property (other than public utility) in one calendar year are levied in the prior calendar year on assessed values listed on December 31 of the prior year, and at tax rates determined in the preceding year. Tangible personal property used in business (except for public utilities) is currently assessed for ad valorem taxation purposes at 25 percent of its true value. Amounts paid by multi-county taxpayers are due September 20. Single county taxpayers may pay annually or semi-annually. If paid annually, payment is due April 30; if paid semi-annually, the first payment is due April 30 with the remainder payable by September 20.

Public utility real and tangible personal property taxes collected in one calendar year are levied in the preceding calendar year on assessed values determined as of December 31 of the second year preceding the tax collection year, the lien date. Certain public utility tangible personal property currently is assessed at 88 percent of its true value; public utility real property is assessed at 35 percent of true value. Public utility property taxes are payable on the same dates as real property taxes described previously.

The County Treasurer collects property taxes on behalf of all taxing districts in the County, including the City of Defiance. The County Auditor periodically remits to the City its portion of the taxes collected. The full tax rate for all City operations for the year ended December 31, 2004 was \$10.59 per \$1,000 of assessed value. The assessed values of real and tangible personal property upon which 2003 property tax receipts were based are as follows:

Real property tax	\$ 155,337,430
Public utility tangible personal property	64,953,670
Tangible personal property	<u>52,271,453</u>
Total assessed valuation	<u><u>\$ 272,562,553</u></u>

Property taxes receivables represent real and tangible personal property taxes, public utility taxes and outstanding delinquencies which are measurable as of December 31, 2004. Although total property tax collections for the next year are measurable, they are generally not collected during the available period. The exception to this is any advances received by the City in the first thirty-one days of the year are credited as property tax revenues with the remainder being credited to deferred revenue.

CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 7 - LOCAL INCOME TAX

This locally levied tax of 1.3 percent is applied to gross salaries, wages and other personal service compensation earned by residents both in and out of the City, and to earnings of nonresidents (except certain transients) earned in the City. It also applies to net income of for-profit organizations conducting business within the City. Income tax revenue is reported to the extent that it was measurable and available to finance current operations at December 31. Income tax revenue for 2004 was \$5,944,049.

NOTE 8 - RECEIVABLES

Receivables at December 31, 2004, consisted of income and property taxes, accounts (billings for user charged services), special assessments, and intergovernmental receivables arising from grants, entitlements, and shared revenue. All intergovernmental receivables have been classified as "Due From Other Governments" on the BFS. Receivables have been recorded to the extent that they are measurable at December 31, 2004, as well as intended to finance fiscal 2004 operations.

A summary of the principal items of receivables reported on the statement of net assets follows:

Governmental Activities:

Income taxes	\$1,635,926
Property and other local taxes	834,894
Accounts	408,268
Special assessments	592,188
Due from other governments	2,179,673

Business-type Activities:

Accounts	300,233
Special assessments	239,407
Due from other governments	1,190

Receivables have been disaggregated on the face of the BFS. The only receivable not expected to be collected within the subsequent year are the special assessments which are collected over the life of the assessment.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 9 - CAPITAL ASSETS

- A. The capital asset balances of the governmental activities have been restated due to the reporting of errors and omissions of capital assets in the prior year. Under GASB Statement No. 34, the City has elected to “phase in” the retroactive reporting of governmental infrastructure assets. The City plans to retroactively report infrastructure capital assets in the 2005 basic financial statements. Only governmental infrastructure capital assets acquired or constructed in 2003 and 2004 are reflected in the basic financial statements for the fiscal year ended December 31, 2004.

	Balance		Restated
<u>Governmental Activities:</u>	<u>12/31/03</u>	<u>Adjustments</u>	<u>Balance</u>
			<u>01/01/04</u>
Land	\$ 1,243,358	\$ 201,361	\$ 1,444,719
Land improvements	979,424	-	979,424
Buildings and improvements	4,517,525	-	4,517,525
Furniture and equipment	2,031,019	-	2,031,019
Vehicles	2,270,869	-	2,270,869
Infrastructure	301,608	-	301,608
Less: accumulated depreciation	<u>(5,658,253)</u>	<u>-</u>	<u>(5,658,253)</u>
Total	<u>\$ 5,685,550</u>	<u>\$ 201,361</u>	<u>\$ 5,886,911</u>

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 9 - CAPITAL ASSETS - (Continued)

B. Capital asset activity for the year ended December 31, 2004, was as follows:

	Restated Balance 01/01/04	<u>Additions</u>	<u>Disposals</u>	Balance 12/31/04
<u>Governmental Activities:</u>				
<i>Capital assets, not being depreciated:</i>				
Land	\$ 1,444,719	\$ -	\$ (201,361)	\$ 1,243,358
Total capital assets, not being depreciated	<u>1,444,719</u>	<u>-</u>	<u>(201,361)</u>	<u>1,243,358</u>
<i>Capital assets, being depreciated:</i>				
Buildings	4,517,525	5,900	-	4,523,425
Improvements other than buildings	979,424	-	-	979,424
Equipment	2,031,019	18,738	(11,570)	2,038,187
Vehicles	2,270,869	68,467	(21,087)	2,318,249
Infrastructure	<u>301,608</u>	<u>-</u>	<u>-</u>	<u>301,608</u>
Total capital assets, being depreciated	<u>10,100,445</u>	<u>93,105</u>	<u>(32,657)</u>	<u>10,160,893</u>
<i>Less: accumulated depreciation:</i>				
Buildings	(2,669,486)	(123,719)	-	(2,793,205)
Improvements other than buildings	(594,419)	(39,339)	-	(633,758)
Equipment	(711,773)	(106,187)	11,325	(806,635)
Vehicles	(1,677,548)	(129,024)	15,816	(1,790,756)
Infrastructure	<u>(5,027)</u>	<u>(5,027)</u>	<u>-</u>	<u>(10,054)</u>
Total accumulated depreciation	<u>(5,658,253)</u>	<u>(403,296)</u>	<u>27,141</u>	<u>(6,034,408)</u>
Total capital assets, being depreciated, net	<u>4,442,192</u>	<u>(310,191)</u>	<u>(5,516)</u>	<u>4,126,485</u>
Governmental activities capital assets, net	<u>\$ 5,886,911</u>	<u>\$ (310,191)</u>	<u>\$ (206,877)</u>	<u>\$ 5,369,843</u>

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 9 - CAPITAL ASSETS - (Continued)

<u>Business-type Activities:</u>	<u>Balance</u> <u>01/01/04</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance</u> <u>12/31/04</u>
<i>Capital assets, not being depreciated:</i>				
Land	\$ 267,100	\$ -	\$ -	\$ 267,100
Construction in progress	<u>923,903</u>	<u>1,412,794</u>	<u>(467,843)</u>	<u>1,868,854</u>
Total capital assets, not being depreciated	<u>1,191,003</u>	<u>1,412,794</u>	<u>(467,843)</u>	<u>2,135,954</u>
<i>Capital assets, being depreciated:</i>				
Land improvements	789,494	-	-	789,494
Buildings and improvements	29,467,691	7,102	-	29,474,793
Equipment	2,321,770	-	-	2,321,770
Vehicles	802,796	8,051	-	810,847
Infrastructure	<u>24,610,128</u>	<u>370,742</u>	<u>-</u>	<u>24,980,870</u>
Total capital assets, being depreciated	<u>57,991,879</u>	<u>385,895</u>	<u>-</u>	<u>58,377,774</u>
<i>Less: accumulated depreciation:</i>				
Land improvements	(329,650)	(27,712)	-	(357,362)
Buildings and improvements	(6,366,038)	(692,888)	-	(7,058,926)
Equipment	(2,010,684)	(69,834)	-	(2,080,518)
Vehicles	(549,213)	(73,928)	-	(623,141)
Infrastructure	<u>(9,425,765)</u>	<u>(445,908)</u>	<u>-</u>	<u>(9,871,673)</u>
Total accumulated depreciation	<u>(18,681,350)</u>	<u>(1,310,270)</u>	<u>-</u>	<u>(19,991,620)</u>
Total capital assets, being depreciated, net	<u>39,310,529</u>	<u>(924,375)</u>	<u>-</u>	<u>38,386,154</u>
Business-type activities capital assets, net	<u>\$ 40,501,532</u>	<u>\$ 488,419</u>	<u>\$ (467,843)</u>	<u>\$ 40,522,108</u>

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 9 - CAPITAL ASSETS - (Continued)

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

Governmental activities:

General government	\$ 46,795
Security of persons and property	106,580
Public health and welfare	41,039
Transportation	70,305
Community environment	24,563
Leisure time activity	<u>114,014</u>
Total depreciation expense - governmental activities	<u>\$ 403,296</u>

NOTE 10 - OTHER EMPLOYEE BENEFITS

Compensated Absences

Accumulated Unpaid Vacation

City employees earn vacation leave at varying rates based upon length of service. In the case of death or retirement, an employee (or his estate) is paid for his unused vacation leave. The total obligation for vacation leave for the City as a whole amounted to \$300,948 at December 31, 2004. Amounts are recorded as a fund liability and/or on the government-wide financial statements as applicable.

Accumulated Unpaid Sick Leave

City employees earn sick leave at varying rates based upon length of service. Upon retirement an employee is paid a percentage of his accumulated sick leave within various limits. The total obligation for sick leave accrual for the City as a whole amounted to \$477,078 at December 31, 2004. Amounts are recorded as a fund liability and/or on the government-wide financial statements as applicable.

NOTE 11 - NOTES PAYABLE

The City had the following bond anticipation notes outstanding at December 31, 2004:

	Issue	Balance			Balance
Governmental Activities:	<u>Date</u>	<u>01/01/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>12/31/04</u>
General Obligation Bond					
<u>Anticipation Notes:</u>					
Capital Improvements Fund - 2003	12/24/03	\$ 835,000	\$ -	\$ (835,000)	\$ -
Capital Improvements Fund - 2004	12/24/04	<u>-</u>	<u>835,000</u>	<u>-</u>	<u>835,000</u>
Capital Improvements Fund	12/24/03	<u>\$ 835,000</u>	<u>\$ 835,000</u>	<u>\$(835,000)</u>	<u>\$ 835,000</u>

On December 24, 2004, the City issued \$835,000 of general obligation bonds anticipation notes for the purpose of improving the streets within the Powell View subdivision. The notes have a maturity date of December 24, 2005.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 11 - NOTES PAYABLE - (Continued)

The City had the following bond anticipation note activity during fiscal year 2004 in the Water and Sewer enterprise funds:

<u>Business-Type Activities</u>	<u>Interest Rate</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Balance 01/01/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 12/31/04</u>
<u>Sewer Fund</u>							
Utilities improvement	1.80%	05/09/03	05/09/04	\$ 113,000	\$ -	\$ (113,000)	\$ -
Sewer improvements - 2003	1.25%	07/12/03	07/11/04	1,698,000	-	(1,698,000)	-
Sewer improvements - 2004	1.25%	07/11/04	07/11/05	-	1,465,000	-	1,465,000
Total Sewer				<u>\$ 1,811,000</u>	<u>\$ 1,465,000</u>	<u>\$ (1,811,000)</u>	<u>\$ 1,465,000</u>
<u>Water Fund</u>							
Utilities improvement	1.80%	05/09/03	05/09/04	\$ 113,000	\$ -	\$ (113,000)	\$ -
Total Water				<u>\$ 113,000</u>	<u>\$ -</u>	<u>\$ (113,000)</u>	<u>\$ -</u>

NOTE 12 - LONG-TERM OBLIGATIONS

A. Governmental Activities Long-Term Obligations

The City's long term obligations for the governmental activities at year-end consist of the following:

<u>Governmental Activities:</u>	<u>Balance 01/01/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 12/31/04</u>	<u>Amount Due in One Year</u>
Compensated absences payable	\$ 539,250	\$ 291,706	\$ (268,777)	\$ 562,179	\$ 220,501
General obligation bonds payable	290,000	-	(30,000)	260,000	30,000
Special assessment bonds payable	618,154	-	(71,967)	546,187	72,967
Bond anticipation notes payable	<u>760,000</u>	<u>760,000</u>	<u>(760,000)</u>	<u>760,000</u>	<u>760,000</u>
Total	<u>\$ 2,207,404</u>	<u>\$ 1,051,706</u>	<u>\$ (1,130,744)</u>	<u>\$ 2,128,366</u>	<u>\$ 1,083,468</u>

Special assessment debt with governmental commitment and debt issued for governmental purposes of the City is retired from the debt service fund. General obligation bonds are secured by the City's ability to levy a voted or unvoted property tax within limitations of Ohio law.

Special assessment bonds are secured by an unvoted property tax levy (special assessment), however, each appropriate bond indenture provides for principal and interest to be paid from use charges.

On July 13, 2000, the City issued \$760,000 in bond anticipation notes to pay costs of acquiring, remodeling, and renovating a building and site to house municipal functions. In 2001, the City issued a \$762,000 bonds anticipation note to retire the previous note and provide funds to continue the construction process. In 2002, the City issued a \$762,388 bond anticipation note to retire the previous note and provide funds to continue the construction process. In 2003, the City issued a \$760,000 bond anticipation note to retire the previous note and provide funds to continue the construction process. In 2004, the City issued a \$760,000 bond anticipation note to retire the previous note and provide funds to continue the construction process.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 12 - LONG-TERM OBLIGATIONS - (Continued)

The proceeds of the 2004 issue and the retirement of the 2003 issue are reported in the general fund.

The following is a summary of the City's future annual debt service requirements for the governmental activities long-term obligations:

<u>Year Ending</u>	<u>General Obligation Bonds</u>			<u>Special Assessment Bonds</u>		
	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 30,000	\$ 18,070	\$ 48,070	\$ 72,967	\$ 37,026	\$ 109,993
2006	35,000	15,985	50,985	77,968	32,136	110,104
2007	35,000	13,553	48,553	77,968	26,491	104,459
2008	40,000	11,120	51,120	87,968	21,131	109,099
2009	40,000	8,348	48,348	62,958	15,007	77,965
2010-2014	<u>80,000</u>	<u>7,948</u>	<u>87,948</u>	<u>166,358</u>	<u>22,614</u>	<u>188,972</u>
Total	<u>\$ 260,000</u>	<u>\$ 75,024</u>	<u>\$ 335,024</u>	<u>\$ 546,187</u>	<u>\$ 154,405</u>	<u>\$ 700,592</u>

B. Business-Type Activities Long-Term Obligations

The City had the following general obligation bonds and long-term loans payable outstanding at year-end related to business-type activities:

<u>Business-Type Activities</u>	<u>Interest Rate</u>	<u>Balance 01/01/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 12/31/04</u>	<u>Amount Due in One Year</u>
<u>General Obligation Bonds:</u>						
Waterline improvements	6.10%	\$ 4,965,000	\$ -	\$ (160,000)	\$ 4,805,000	\$ 185,000
Waterworks - Series 1997	Various	<u>7,035,000</u>	<u>-</u>	<u>(215,000)</u>	<u>6,820,000</u>	<u>225,000</u>
Total general obligation bonds		<u>12,000,000</u>	<u>-</u>	<u>(375,000)</u>	<u>11,625,000</u>	<u>410,000</u>
<u>Special Assessment Bonds</u>						
Sewer street improvements - Series 2000	5.75%	<u>134,901</u>	<u>-</u>	<u>(4,888)</u>	<u>130,013</u>	<u>5,169</u>
<u>Other Long-Term Obligations</u>						
OWDA loan	3.91-7.65%	12,873,756	-	(728,614)	12,145,142	772,816
OPWC loan	0-4.00%	1,056,313	-	(68,208)	988,105	69,510
Compensated absence payable		<u>257,576</u>	<u>61,011</u>	<u>(102,740)</u>	<u>215,847</u>	<u>93,744</u>
Total other long-term obligations		<u>14,187,645</u>	<u>61,011</u>	<u>(899,562)</u>	<u>13,349,094</u>	<u>936,070</u>
Total business-type activities long-term liabilities		<u>\$ 26,322,546</u>	<u>\$ 61,011</u>	<u>\$ (1,279,450)</u>	<u>\$ 25,104,107</u>	<u>\$ 1,351,239</u>

General obligation bonds are expected to be retired with revenues of the enterprise funds. General obligation bonds are secured by the City's ability to levy a voted or unvoted property tax within limitations of Ohio law.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 12 - LONG-TERM OBLIGATIONS - (Continued)

On February 3, 1998, the City issued \$8,000,000 in Waterworks System Improvements bonds. The Bonds were issued for the purpose of improving and expanding the municipal waterworks system by acquiring, construction, reconstructing and otherwise improving structures and facilities for raw water intake, treatment and storage, finished water storage and distribution and waterworks administration and service, including all necessary equipment, site improvements and furnishings, together with all necessary and related improvements and the acquisition of any real estate or interest therein required. During 2004, the City retired \$215,000 of these bonds, leaving an outstanding balance of \$6,820,000 at December 31, 2004.

On May 11, 2001, the City issued \$145,434 in special assessment bonds to finance the costs of sewer improvements to South Jefferson Street. These bonds bear an interest rate of 5.75 percent and mature December 1, 2020. During 2004, the City retired \$4,888 of these bonds, leaving an outstanding balance of \$130,013 at December 31, 2004.

The City constructed a waste water treatment facility in 1990. The Project was financed through expenditure by the Ohio Water Development Authority (OWDA). In 1999, the City began making major improvements to its wastewater treatment facility, which were also partially financed by OWDA. At December 31, 2004, the City had the following OWDA loans outstanding:

	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Balance Outstanding 12/31/04</u>
OWDA loan	7.65%	1/1/2013	\$ 5,104,372
OWDA loan	3.91%	7/1/2020	<u>7,040,770</u>
Total			<u>\$12,145,142</u>

Improvements to the City's water treatment facilities were financed through expenditures by the Ohio Public Works Commission (OPWC). At December 31, 2004, the City has the following four loans outstanding to the OPWC:

	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Balance Outstanding 12/31/04</u>
OPWC loan	4.00%	1/1/2014	\$ 191,628
OPWC loan	3.00%	7/1/2017	346,298
OPWC loan	3.91%	7/1/2019	284,180
OPWC loan	3.91%	7/1/2020	<u>165,999</u>
Total			<u>\$ 988,105</u>

The loans are payable in semi-annual installments of principal and interest (if applicable).

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 12 - LONG-TERM OBLIGATIONS - (Continued)

The following is a summary of the City's future annual debt service principal and interest requirements for the business-type activities:

Year Ending	General Obligation Bonds			Sewer Special Assessment Bonds		
	Principal	Interest	Total	Principal	Interest	Total
2005	\$ 410,000	\$ 650,525	\$ 1,060,525	\$ 5,169	\$ 7,476	\$ 12,645
2006	430,000	630,583	1,060,583	5,467	7,178	12,645
2007	455,000	609,108	1,064,108	5,781	6,864	12,645
2008	475,000	586,007	1,061,007	6,113	6,532	12,645
2009	505,000	561,113	1,066,113	6,465	6,180	12,645
2010-2014	2,970,000	2,328,700	5,298,700	38,346	24,879	63,225
2015-2019	3,905,000	1,350,000	5,255,000	50,714	12,511	63,225
2020-2023	2,475,000	287,460	2,762,460	11,958	687	12,645
Total	<u>\$ 11,625,000</u>	<u>\$ 7,003,496</u>	<u>\$ 18,628,496</u>	<u>\$ 130,013</u>	<u>\$ 72,307</u>	<u>\$ 202,320</u>

Year Ending	OWDA Loans Payable			OPWC Loans Payable		
	Principal	Interest	Total	Principal	Interest	Total
2005	\$ 772,816	\$ 662,642	\$ 1,435,458	\$ 69,510	\$ 17,751	\$ 87,261
2006	819,944	615,514	1,435,458	70,857	16,404	87,261
2007	870,205	565,253	1,435,458	72,252	15,009	87,261
2008	923,818	511,640	1,435,458	73,696	13,565	87,261
2009	981,020	454,437	1,435,457	75,191	12,070	87,261
2010-2014	4,616,634	1,244,102	5,860,736	399,564	36,026	435,590
2015-2019	2,581,695	398,850	2,980,545	221,686	3,632	225,318
2020	579,010	17,099	596,109	5,349	-	5,349
Total	<u>\$ 12,145,142</u>	<u>\$ 4,469,537</u>	<u>\$ 16,614,679</u>	<u>\$ 988,105</u>	<u>\$ 114,457</u>	<u>\$ 1,102,562</u>

NOTE 13 - RISK MANAGEMENT

The City is exposed to various risks of loss related to torts, theft of, and destruction of assets, errors and omissions, injuries to employees and natural disasters. The City participates with other cities in the Buckeye Ohio Risk Management Agency, Inc. (BORMA, Inc.), in jointly funded risk financing programs administered by Arthur J. Gallagher & Co. BORMA, Inc. includes two separate pools which provide separate and distinct coverages.

The first pool provides comprehensive automobile liability, automobile physical damage, comprehensive general liability, crime and property liability, and public officials' liability coverage up to specific limits. The pool includes the following municipalities: Archbold, Bowling Green, Defiance, Huron, Napoleon, Sandusky and Willard. Member contributions are calculated annually to produce a sufficient sum of money within the pool to fund administrative expenses and to create reserves for claims. As of December 31, 2004, the pool had cash reserves of \$601,551, which in the opinion of management is adequate for any claims against the pool. The amount of risk retained with the pool is \$300,000 per claim.

Claims in excess of the \$300,000 up to \$10,000,000 are covered by various insurance carriers.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 13 - RISK MANAGEMENT - (Continued)

The second pool is for employee benefits and includes life insurance, accidental death and dismemberment insurance, health insurance and prescription drug insurance. Each member has an option on the coverage it has elected to provide for its employees. Defiance provides to its employees all available options offered by the pool. The employee benefits pool includes the following municipalities: Archbold, Bowling Green, Carey, Clyde, Defiance, Fayette, Hicksville, Napoleon, Oberlin, Sandusky, Upper Sandusky and Willard. As of December 31, 2004 the pool had cash reserves of \$2,397,520 which, in the opinion of management, is adequate for any claims against the pool.

Premiums are paid to the employee benefits pool at a cost of \$966.97 for family coverage, \$726.18 for two party coverage, and \$335.84 for single party coverage. Life insurance monthly premiums are \$4.72 for family and two party coverage and \$2.60 for single party coverage. During 2004, the City paid \$1,249,325 into the pool for coverage. The cost of coverage is paid by the fund that pays the salary of the individual employees. The amount of the risk retained within the employee is \$75,000 per individual with excess claims coverage provided by the Lloyds Company.

BORMA, Inc. has the ability to require the member cities to make supplemental payments in the event reserves are not adequate to cover claims. The probability of this occurring is considered remote due to the adequacy of the pool reserves and premium levels, therefore, no amount have been reserved in the financial statements. Audited financial statements are maintained separately by BORMA, Inc.

Workers' Compensation claims are covered through the City's participation in the State of Ohio's program. The City pays the State Workers' Compensation System a premium based upon a rate per \$100 of payroll plus administrative costs. The rate is determined based on accident history of the North Central Ohio Municipal Finance Officers Association, of which the City is a member. The City also pays unemployment claims to the State of Ohio as incurred.

There has been no significant reduction in insurance coverages from coverages in the prior year. In addition, settled claims resulting from these risks have not exceeded commercial insurance converge in any of the past three fiscal years.

NOTE 14 - DEFINED BENEFIT PENSION PLANS

A. Ohio Public Employees Retirement System

The City participates in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans. The traditional plan is a cost-sharing, multiple-employer defined benefit pension plan. The member-directed plan is a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the member directed plan, members accumulate retirement assets equal to the value of the member and vested employer contributions plus any investment earnings. The combined plan is a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and a defined contribution plan. Under the combined plan, employer contributions are invested by the retirement system to provide a formula retirement benefit similar to the traditional plan benefit. Member contributions, whose investment is self-directed by the member, accumulate retirement assets in a manner similar to the member directed plan.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 14 - DEFINED BENEFIT PENSION PLANS - (Continued)

OPERS provides retirement, disability, survivor and death benefits and annual cost of living adjustments to members of the traditional and combined plans. Members of the member directed plan do not qualify for ancillary benefits. Authority to established and amend benefits is provided by Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that may be obtained by writing to OPERS, 277 E. Town St., Columbus, OH 43215-4642 or by calling (614) 222-6705.

For the year ended December 31, 2004, the members of all three plans, except those in law enforcement or public safety participating in the traditional plan, were required to contribute 8.5% of their annual covered salaries. Members participating in the traditional plan who were in law enforcement contributed 10.1% of their annual covered salary; members in public safety contributed 9%. The City's contribution rate for pension benefits for 2004 was 9.55%, except for those plan members in law enforcement or public safety. For those classifications, the City's pension contributions were 12.7% of covered payroll. The Ohio Revised Code provides statutory authority for member and employer contributions.

The City's required contributions for pension obligations to the traditional and combined plans for the years ended December 31, 2004, 2003, and 2002 were \$334,381, \$336,553, and \$568,818, respectively; 93.58% has been contributed for 2004 and 100% for 2003 and 2002. \$34,038, representing the unpaid contribution for 2004, is recorded as a liability within the respective funds. The City and plan members did not make any contributions to the member-directed plan for 2004.

B. Ohio Police and Fire Pension Fund

The City contributes to the Ohio Police and Fire Pension Fund (OP&F), a cost-sharing multiple-employer defined benefit pension plan. OP&F provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by the Ohio State Legislature and are codified in Chapter 742 of the Ohio Revised Code. OP&F issues a publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by writing to the Ohio Police and Fire Pension Fund, 140 East Town Street, Columbus, Ohio 43215-5164.

Plan members are required to contribute 10.0% of their annual covered salary to fund pension obligations while the City is required to contribute 11.75% for police officers and 16.25% for firefighters. Contributions are authorized by State statute. The City's contributions to the Fund for police and firefighters for the years ended December 31, 2004, 2003, and 2002 were \$330,188, \$330,386, and \$343,180, respectively. 93.14% has been contributed for 2004 and 100% for the years 2003 and 2002. \$35,491, representing the unpaid contributions for 2004, is recorded as a liability within the respective funds.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 15 - POSTRETIREMENT BENEFIT PLANS

A. Ohio Public Employees Retirement System

The Ohio Public Employees Retirement System (OPERS) provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit with either the traditional or combined plans. Health care coverage for disability recipients and primary survivor recipients is available. Members of the member-directed plan do not qualify for postretirement health care coverage. The health care coverage provided by the retirement system is considered an Other Postemployment Benefit as described in GASB Statement No. 12, "Disclosure of Information on Postemployment Benefits other than Pension Benefits by State and Local Government Employers". A portion of each employer's contribution to the traditional or combined plans is set aside for the funding of postretirement health care based on authority granted by State statute. The 2004 local government employer contribution rate was 13.55% of covered payroll (16.70% for public safety and law enforcement); 4.00% of covered payroll was the portion that was used to fund health care.

Benefits are advance-funded using the entry age normal actuarial cost method. Significant actuarial assumptions, based on OPER's latest actuarial review performed as of December 31, 2003, include a rate of return on investments of 8.00%, an annual increase in active employee total payroll of 4.00% compounded annually (assuming no change in the number of active employees) and an additional increase in total payroll of between .50% and 6.3% based on additional annual pay increases. Health care premiums were assumed to increase 4.00% annually.

All investments are carried at market. For actuarial valuation purposes, a smoothed market approach is used. Assets are adjusted to reflect 25% of unrealized market appreciation or depreciation on investment assets annually.

The number of active contributing participants in the traditional and combined plans was 369,885. Actual employer contributions for 2004 which were used to fund postemployment benefits were \$195,545. The actual contribution and the actuarially required contribution amounts are the same. OPERS's net assets available for payment of benefits at December 31, 2003 (the latest information available) were \$10.5 billion. The actuarially accrued liability and the unfunded actuarial accrued liability were \$26.9 billion and \$16.4 billion, respectively.

In December 2001, the Board adopted the Health Care "Choices" Plan. The Choices Plan will be offered to all persons newly hired in an OPERS covered position after January 1, 2003, with no prior service credit accumulated toward health care coverage. Choices will incorporate a cafeteria approach, offering a broader range of health care options. The Plan uses a graded scale from ten to thirty years to calculate a monthly health care benefit. This is in contrast to the ten-year "cliff" eligibility standard for the present Plan.

The benefit recipient will be free to select the option that best meets their needs. Recipients will fund health care costs in excess of their monthly health care benefit. The Plan will also offer a spending account feature, enabling the benefit recipient to apply their allowance toward specific medical expenses, much like a Medical Spending Account.

On September 9, 2004 the OPERS Retirement Board adopted a Health Care Preservation Plan (HCPP) with an effective date of January 1, 2007. The HCPP restructures OPERS' health care coverage to improve the financial solvency of the fund in response to skyrocketing health care costs.

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 15 - POSTRETIREMENT BENEFIT PLANS - (Continued)

Under the HCPP, retirees eligible for health care coverage will receive a graded monthly allocation based on their years of service at retirement. The Plan incorporates a cafeteria approach, offering a broad range of health care options that allow benefit recipients to use their monthly allocation to purchase health care coverage customized to meet their individual needs. If the monthly allocation exceeds the cost of the options selected, the excess is deposited into a Retiree Medical Account that can be used to fund future health care expenses.

B. Ohio Police and Fire Pension Fund

The Ohio Police and Fire Pension Fund (OP&F) provides postretirement health care coverage to any person who receives or is eligible to receive a monthly service, disability or survivor benefit check or is a spouse or eligible dependent child of such person. An eligible dependent child is any child under the age of 18 whether or not the child is attending school, or under the age of 22 if attending school full-time or on a 2/3 basis.

The health care coverage provided by the retirement system is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12, "Disclosure of Information on Postemployment Benefits other than Pension Benefits by State and Local Government Employers". The Ohio Revised Code provides the authority allowing the Ohio Police and Fire Pension Fund's board of trustees to provide health care coverage and states that health care costs paid from the funds of OP&F shall be included in the employer's contribution rate. Health care funding and accounting is on a pay-as-you-go basis. The total police employer contribution rate is 19.5% of covered payroll and the total firefighter employer contribution rate is 24% of covered payroll, of which 7.75% of covered payroll was applied to the postemployment health care program during 2004. In addition, since July 1, 1992, most retirees have been required to contribute a portion of the cost of their health care coverage through a deduction from their monthly benefit payment. Beginning in 2001, all retirees and survivors have monthly health care contributions.

The City's actual contributions for 2004 that were used to fund postemployment benefits was \$108,190 for police and \$79,132 for firefighters. The OP&F's total health care expense for the year ended December 31, 2003 (the latest information available) was \$150,853,148, which was net of member contributions of \$17,207,506. The number of OP&F participants eligible to receive health care benefits as of December 31, 2003 (the latest information available), was 13,662 for police and 10,474 for firefighters.

NOTE 16 - BUDGETARY BASIS OF ACCOUNTING

While the City is reporting financial position, results of operations and changes in fund balance on the basis of generally accepted accounting principles (GAAP), the budgetary basis as provided by law is based upon accounting for certain transactions on a basis of cash receipts, disbursements and encumbrances. The Statement of Revenues, Expenditures and Changes in Fund Balances - Budget and Actual (Non-GAAP Budgetary Basis) presented for the general fund is presented on the budgetary basis to provide a meaningful comparison of actual results with the budget. The major differences between the budget basis and GAAP basis are as follows:

1. Revenues and other financing sources are recorded when received in cash (budget) as opposed to when susceptible to accrual (GAAP).
2. Expenditures/expenses and other financing uses are recorded when paid in cash (budget) as opposed to when the liability is incurred (GAAP).

CITY OF DEFIANCE, OHIO

NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004

NOTE 16 - BUDGETARY BASIS OF ACCOUNTING - (Continued)

3. Encumbrances are treated as expenditures (budget) rather than as a reservation of fund balance (GAAP).
4. Unreported cash represents amounts received but not included as revenue on the budget basis operating statements. These amounts are included as revenue on the GAAP basis operating statement.

The following table summarizes the adjustments necessary to reconcile the GAAP basis statements (as reported in the fund financial statements) to the budgetary basis statements for all governmental funds for which a budgetary basis statement is presented.

Net Change in Fund Balance

	<u>General</u>
Budget basis	\$ 37,284
Net adjustment for revenue accruals	210,091
Net adjustment for expenditure accruals	337,284
Net adjustment for other sources/uses and extraordinary item	(271,459)
Adjustment for encumbrances	<u>244,607</u>
GAAP basis	<u>\$ 557,807</u>

NOTE 17 - LOANS RECEIVABLE

Loans receivable represent low interest loans made by the City for development projects and businesses under the Community Development Block Grant (CDBG) Program. A summary of the loan activity is as follows:

	Balance Outstanding <u>1/1/2004</u>	Loans Disbursed	Principal Received	Balance Outstanding <u>12/31/04</u>
CDBG loans	<u>\$ 954,374</u>	<u>\$ 255,000</u>	<u>\$ (294,598)</u>	<u>\$ 914,776</u>

The CDBG loans are reported in the nonmajor governmental funds. Fund balance has been reserved for the outstanding balance due at year-end.

CITY OF DEFIANCE, OHIO

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2004**

NOTE 18 - CONTINGENCIES

A. Grants

The City receives significant financial assistance from numerous federal and state agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the general fund or other applicable funds. However, in the opinion of management, any such disallowed claims will not have a material effect on any of the financial statements of the individual fund types included herein or on the overall financial position of the City at December 31, 2004.

B. Litigation

Several claims and lawsuits are pending against the City. In the opinion of the City Law Director, any potential liability would not have a material effect on the Basic Financial Statements.

JULIAN & GRUBE, INC.

“SERVING OHIO LOCAL GOVERNMENTS”

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

Members of Council and Mayor
City of Defiance
631 Perry Street
Defiance, OH 43082

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Defiance, Defiance County, Ohio, (the “City”) as of and for the year ended December 31, 2004, which collectively comprise the City’s basic financial statements and have issued our report thereon dated September 9, 2005. As disclosed in Note 3, the City restated capital assets for errors and omissions. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City’s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that do not require inclusion in this report that we have reported to the management of the City in a separate letter dated September 9, 2005.

Members of Council and Mayor
City of Defiance

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* which are described in accompanying schedule of findings as items 2004-COD-001, 2004-COD-002, and 2004-COD-003. We also noted other matters that we have communicated to management in a separate letter dated September 9, 2005.

This report is intended solely for the information and use of Council and the management of the City of Defiance, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Julian & Grube, Inc.".

Julian & Grube, Inc.
September 9, 2005

**CITY OF DEFIANCE
DEFIANCE COUNTY, OHIO**

**SCHEDULE OF FINDINGS
DECEMBER 31, 2004**

**FINDINGS RELATED TO THE BASIC FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS**

Finding Number	2004-COD-001
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Ohio Revised Code Section 5705.39 states in part that the total appropriation from each fund shall not exceed total estimated resources. It was noted that the following fund had appropriations which exceeded estimated resource at January 1, 2004:

Major/Non-Major Funds	Appropriations	Estimated Resources	Excess
General Fund (Major)	\$8,716,436	\$8,129,861	\$586,575

It was noted that the following funds had appropriations which exceeded estimated resource at December 31, 2004:

Major/Non-Major Funds	Appropriations	Estimated Resources	Excess
General Fund (Major)	\$8,864,201	\$8,129,861	\$734,340
Street Construction, Maintenance and Repair (Non-Major)	847,842	534,432	288,798
Special Projects Fund (Non-Major)	80,000	0	80,000
Cable TV Contract Fee Fund (Non-Major)	24,400	18,743	5,657
Housing Rehabilitation (Non-Major)	375,000	57,457	317,543
Sewer Fund (Major)	7,679,805	6,880,128	799,677
Water Fund (Major)	4,427,854	3,808,789	619,065
Tax Reduction (Non-Major)	32,200	0	32,300
Police Pension (Non-Major)	285,600	259,479	26,121
Fire Damage Repair (Non-Major)	34,000	29,100	4,900

With appropriations exceeding estimated resources, the City is appropriating monies that were not certified by the County Budget Commission. This may result in a fund deficit if not corrected throughout the year.

We recommend that the City comply with the Ohio Revised Code and Auditor of State Bulletin 97-010 by comparing adopted appropriations against certified estimated resources on a continual basis, including amending estimated resources for any changes during the year. If it is determined that estimated resources will be greater than initially anticipated, the City should amend its official estimate in order to provide for any additional appropriations; however, appropriations should not exceed estimated resources.

Client Response: The client will monitor appropriations versus estimated resources throughout the year to determine compliance with the Ohio Revised Code at year-end.

**CITY OF DEFIANCE
DEFIANCE COUNTY, OHIO**

**SCHEDULE OF FINDINGS
DECEMBER 31, 2004**

**FINDINGS RELATED TO THE BASIC FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS**

Finding Number	2004-COD-002
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Ohio Revised Code Section 5705.41(B) requires that no subdivision is to expend money unless it has been appropriated.

It was noted during the audit that the City had expenditures exceeding appropriations in the following funds at December 31, 2004:

<u>Major Fund</u>	<u>Appropriations</u>	<u>Expenditures</u>	<u>Excess</u>
General			
City Administrator			
Operating	\$ 48,283	\$ 88,821	\$ 40,538
Finance			
Debt Service	-	768,660	768,660
Law			
Salaries and Wages	162,432	165,882	3,450
Employee Benefits	39,284	40,904	1,620
Fire			
Employee Benefits	219,331	223,701	4,370
Engineering			
Salaries and Wages	92,478	97,311	4,833
Employee Benefits	31,699	33,199	1,500
Capital Improvement			
Capital Outlay	2,724,952	2,843,213	118,261

With expenditures exceeding appropriations, the City is expending monies that have not been appropriated and approved by Council. This may result in unnecessary purchases or overspending which may lead to a fund deficit.

We recommend that the District comply with the Ohio Revised Code and the Auditor of State Bulletin 97-010 by monitoring expenditures so they do not exceed lawful appropriations and amending the budget throughout the fiscal year. This may be achieved by monitoring the budget more closely on a continual basis.

Client Response: The City will monitor appropriations throughout the year to determine expenditures are within budgeted amounts.

**CITY OF DEFIANCE
DEFIANCE COUNTY, OHIO**

**SCHEDULE OF FINDINGS
DECEMBER 31, 2004**

FINDINGS RELATED TO THE BASIC FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS
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Finding Number	2004-COD-003
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Ohio Revised Code Section 5705.10 in part requires that money paid into any fund shall be expended only after such fund receives monies to cover expenditures.

It was noted during the audit that at December 31, 2004, the City had a negative cash balance in the Permissive Tax Fund of \$151,415.

The City has spent monies not available to that fund and thus causing noncompliance. No fund should have a negative cash fund balance throughout the year or at year end.

We recommend that the City properly record receipts as deposits in transit only after funds have been received and subsequent to proper appropriation. If funds are anticipated, but not yet received and expenditures are necessary, the City should advance or transfer funds from the General Fund with proper Council approval.

Client Response: The City will monitor balances and consider transferring or advancing funds to avoid negative fund balances throughout the year and at year-end.



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CITY OF DEFIANCE

DEFIANCE COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
NOVEMBER 10, 2005**