

CITY OF EAST PALESTINE
ANNUAL REPORT
FOR THE YEAR ENDED DECEMBER 31, 2005

Wolfe, Wilson, & Phillips, Inc.
37 South Seventh Street
Zanesville, Ohio 43701



Mary Taylor, CPA
Auditor of State

City Council
City of East Palestine
82 Garfield Ave.
East Palestine, Ohio 44413

We have reviewed the *Independent Auditors' Report* of the City of East Palestine, Columbiana County, prepared by Wolfe, Wilson & Phillips, Inc., for the audit period January 1, 2005 to December 31, 2005. 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 East Palestine is responsible for compliance with these laws and regulations.

Mary Taylor

Mary Taylor, CPA
Auditor of State

June 6, 2007

This Page is Intentionally Left Blank.

**CITY OF EAST PALESTINE
COLUMBIANA COUNTY**

TABLE OF CONTENTS

<u>Title</u>	<u>Page</u>
Independent Auditors' Report.....	1
Management Discussion and Analysis.....	3
Government-wide Financial Statements:	
Statement of Nets Assets Year Ended December 31, 2005.....	13
Statement of Activities Year Ended December 31, 2005.....	14
Fund Financial Statements:	
Governmental Funds	
Balance Sheet, Year Ended December 31, 2005.....	16
Reconciliation of Total Government Fund Balances to Net Assets of Governmental Activites.....	17
Statement of Revenues, Expenditures and Changes in Fund Balance, Year Ended December 31, 2005.....	18
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance of Governmental Funds to the Statement of Activities.....	19
Statement of Cash Receipts, Disbursements and Changes in Fund Cash Balances- Budget and Actual (Non-GAAP Budgetary Basis) - General Fund, Year Ended December 31, 2005.....	20
Statement of Cash Receipts, Disbursements and Changes in Fund Cash Balances- Budget and Actual (Non-GAAP Budgetary Basis) - FEMA Fund, Year Ended December 31, 2005.....	21
Statement of Cash Receipts, Disbursements and Changes in Fund Cash Balances- Budget and Actual (Non-GAAP Budgetary Basis) - Electric Trust Fund, Year Ended December 31, 2005.....	22
Proprietary Funds	
Statement of Net Assets, Year Ended December 31, 2005.....	23
Statement of Revenues, Expenses and Changes in Fund Net Assets, Year Ended December 31, 2005.....	24
Statement of Cash Flows, Year Ended December 31, 2005.....	25
Fiduciary Funds	
Statement of Assets and Liabilities, Year Ended December 31, 2005.....	26
Notes to the Financial Statements.....	27
Independent Auditors' Report on Compliance and on Internal Control Over Financial Reporting based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.....	54
Independents Auditors' Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133.....	55
Schedule of Findings and Questioned Costs.....	57
Schedule of Federal Awards.....	58
Notes to Schedule of Federal Awards.....	59

This Page is Intentionally Left Blank.

**WOLFE, WILSON, & PHILLIPS, INC.
37 SOUTH SEVENTH STREET
ZANESVILLE, OHIO 43701**

INDEPENDENT AUDITORS' REPORT

City of East Palestine
Columbiana County
82 Garfield Avenue
East Palestine, Ohio 44413

We have audited the accompanying financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of East Palestine, Columbiana County as of and for the year ended December 31, 2005, 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates, if any, made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of East Palestine, Columbiana County as of December 31, 2005, and the respective changes in financial position and cash flows, where applicable, and the respective budgetary comparison for the General Fund, FEMA Fund and Electric Trust Fund for the year then ended in conformity generally accepted accounting principles accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 5, 2007, on our consideration of City of East Palestine's internal control over financial reporting and our tests of its compliance with laws, regulations, contracts and grant agreements and other matters. That report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. It does not opine on the internal control over financial reporting or on compliance. That report is an integral part of an audit in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Management's discussion and analysis is not a required part of the basic financial statements but is supplementary information the Governmental Accounting Standards Board requires. 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.

We conducted our audit to opine of the financial statements that collectively comprise the City's basic financial statements. The accompanying schedule of expenditures of federal awards expenditures present additional information and is required by U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. It is not a required part of the basic financial statements. We subjected the federal awards expenditure schedule to the auditing procedures applied in the audit of the basic financial statements. In our opinion, this information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Wolfe, Wilson, & Phillips, Inc.
Zanesville, Ohio
January 5, 2007

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2005***

Unaudited

The discussion and analysis of the City of East Palestine's financial performance provides an overall review of the City's financial activities for the fiscal year ended December 31, 2005. The intent of this discussion and analysis is to look at the City's financial performance as a whole; readers should also review the notes to the basic financial statements and financial statements to enhance their understanding of the City's financial performance.

FINANCIAL HIGHLIGHTS

Key financial highlights for 2005 are as follows:

- ❑ In total, net assets increased \$783,314. Net assets of governmental activities increased \$711,461, which represents a 21% increase from 2004. Net assets of business-type activities increased \$71,853 or 5% from 2004.
- ❑ General revenues accounted for \$1,702,438 in revenue or 28% of all revenues. Program specific revenues in the form of charges for services and grants and contributions accounted for \$4,444,931, 72% of total revenues of \$6,147,369.
- ❑ The City had \$3,864,927 in expenses related to governmental activities; only \$2,881,908 of these expenses were offset by program specific charges for services, grants or contributions. General revenues of \$1,702,438 were adequate to provide for these programs.
- ❑ Among major funds, the general fund had \$1,759,778 in revenues and other financing sources and \$1,782,204 in expenditures and other financing uses. The general fund's fund balance decreased from a deficit of \$528,550 to a deficit of \$550,976.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts – *management's discussion and analysis* and the *basic financial statements*. The basic financial statements include two kinds of statements that present different views of the City:

These statements are as follows:

The Government-Wide Financial Statements – These statements provide both long-term and short-term information about the City's overall financial status.

The Fund Financial Statements – These statements focus on individual parts of the City, reporting the City's operations in more detail than the government-wide statements.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2005***

Unaudited

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the City's net assets and how they have changed. Net-assets (the difference between the City's assets and liabilities) are one way to measure the City's financial health or position.

- Over time, increases or decreases in the City's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional nonfinancial factors such as the City's tax base and the condition of the City's capital assets

The government-wide financial statements of the City are divided into two categories:

- *Governmental Activities* – Most of the City's program's and services are reported here including security of persons and property, public health and welfare services, leisure time activities, community environment, transportation and general government.
- *Business-Type Activities* – These services are provided on a charge for goods or services basis to recover all of the expenses of the goods or services provided. The City's water and wastewater services are reported as business-type activities.

Fund Financial Statements

Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes. The fund financial statements provide more detailed information about the City's most significant funds, not the City as a whole.

Governmental Funds – Most of the City's activities are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end available for spending in future periods. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is reconciled in the financial statements.

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2005**

Unaudited

Proprietary Funds – Proprietary funds use the same basis of accounting as business-type activities; therefore, these statements will essentially match. The proprietary fund financial statements provide separate information for the Water and Wastewater funds, both of which are considered major funds.

Fiduciary Funds – Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are *not* reflected in the government-wide financial statement because the resources of those funds are *not* available to support the City's own programs. All of the City's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

The following table provides a summary of the City's net assets for 2005 compared to 2004.

	Governmental Activities		Business-type Activities		Total	
	2005	Restated 2004	2005	Restated 2004	2005	Restated 2004
Current and other assets	\$3,274,871	\$1,907,135	\$235,205	\$228,073	\$3,510,076	\$2,135,208
Capital assets, Net	3,709,581	2,384,074	9,408,744	7,139,945	13,118,325	9,524,019
Total assets	6,984,452	4,291,209	9,643,949	7,368,018	16,628,401	11,659,227
Long-term debt outstanding	1,247,724	273,871	7,841,661	5,787,820	9,089,385	6,061,691
Other liabilities	1,603,579	595,650	348,656	198,419	1,952,235	794,069
Total liabilities	2,851,303	869,521	8,190,317	5,986,239	11,041,620	6,855,760
Net assets						
Invested in capital assets, net of related debt	2,685,502	2,271,457	1,918,058	1,760,539	4,603,560	4,031,996
Restricted	3,905,468	3,541,296	0	0	3,905,468	3,541,296
Unrestricted	(2,457,821)	(2,391,065)	(464,426)	(378,760)	(2,922,247)	(2,769,825)
Total net assets	\$4,133,149	\$3,421,688	\$1,453,632	\$1,381,779	\$5,586,781	\$4,803,467

CITY OF EAST PALESTINE, OHIO

Management's Discussion and Analysis For the Year Ended December 31, 2005

Unaudited

Changes in Net Assets – The following table shows the changes in net assets for the fiscal year 2005 compared to 2004:

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Revenues						
Program revenues:						
Charges for Services and Sales	\$383,956	\$444,804	\$1,354,442	\$1,473,864	\$1,738,398	\$1,918,668
Operating Grants and Contributions	1,758,075	524,933	141,581	0	1,899,656	524,933
Capital Grants and Contributions	739,877	105,121	67,000	0	806,877	105,121
Total Program revenues	2,881,908	1,074,858	1,563,023	1,473,864	4,444,931	2,548,722
General revenues:						
Property Taxes	352,252	244,853	0	0	352,252	244,853
Income Taxes	865,543	833,631	0	0	865,543	833,631
Other Local Taxes	506	515	0	0	506	515
Contributions not Restricted to Specific Programs	327,164	256,745	0	0	327,164	256,745
Investment Earnings	22,957	13,217	0	0	22,957	13,217
Miscellaneous	134,016	104,724	0	0	134,016	104,724
Total General revenues	1,702,438	1,453,685	0	0	1,702,438	1,453,685
Total revenues	4,584,346	2,528,543	1,563,023	1,473,864	6,147,369	4,002,407
Program Expenses						
Security of Persons and Property	2,109,466	1,331,317	0	0	2,109,466	1,331,317
Leisure Time Activities	241,259	252,351	0	0	241,259	252,351
Community Environment	374,872	179,414	0	0	374,872	179,414
Public Health and Welfare	45,069	56,424	0	0	45,069	56,424
Transportation	364,062	382,472	0	0	364,062	382,472
General Government	719,460	479,108	0	0	719,460	479,108
Interest and Fiscal Charges	10,739	14,266	0	0	10,739	14,266
Water	0	0	441,212	367,308	441,212	367,308
Wastewater	0	0	1,057,916	1,202,078	1,057,916	1,202,078
Total expenses	3,864,927	2,695,352	1,499,128	1,569,386	5,364,055	4,264,738
Change in Net Assets before transfers	719,419	(166,809)	63,895	(95,522)	783,314	(262,331)
Transfers	(7,958)	(191,227)	7,958	191,227	0	0
Total Change in Net Assets	711,461	(358,036)	71,853	95,705	783,314	(262,331)
Beginning Net Assets-Restated	3,421,688	3,779,724	1,381,779	1,286,074	4,803,467	5,065,798
Ending Net Assets	\$4,133,149	\$3,421,688	\$1,453,632	\$1,381,779	\$5,586,781	\$4,803,467

Governmental Activities

Net assets of the City's governmental activities increased 21% from the previous year. This increase was largely the result of increases in both operating and capital grants and contributions.

The City receives an income tax, which is based on 1% of all salaries, wages, commissions and other compensation and on net profits earned from residents living within the City.

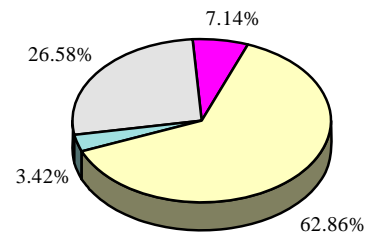
CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2005**

Unaudited

Income taxes and property taxes made up 19% and 8% respectively of revenues for governmental activities for the City in fiscal year 2005. The City's reliance upon tax revenues is demonstrated by the following graph indicating 27% of total revenues from general tax revenues:

Revenue Sources	2005	Percent of Total
General Tax Revenues	\$1,218,301	26.58%
Shared Revenue	327,164	7.14%
Program Revenues	2,881,908	62.86%
General Other	156,973	3.42%
Total Revenue	\$4,584,346	100.00%



Business-Type Activities

Net assets of the business-type activities increased \$71,853. This increase was mainly the result of capital contributions received from the City's Governmental Activities.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The City's governmental funds reported a combined fund balance of \$900,089, which is an increase from last year's balance of \$788,725. The schedule below indicates the fund balance and the total change in fund balance by fund type as of December 31, 2004 and 2005:

	Fund Balance/Deficit December 31, 2005	Fund Balance/Deficit December 31, 2004	Increase (Decrease)
General	(\$550,976)	(\$528,550)	(\$22,426)
FEMA	(120)	34,193	(34,313)
Electric Trust	3,119,168	3,040,000	79,168
Capital Improvement	(1,986,018)	(2,031,292)	45,274
Other Governmental	318,035	274,374	43,661
Total	\$900,089	\$788,725	\$111,364

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2005***

Unaudited

General Fund – The City's General Fund balance decrease is due to several factors. The tables that follow assist in illustrating the financial activities of the General Fund:

	2005 Revenues	2004 Revenues	Increase (Decrease)
Taxes	\$976,392	\$924,235	\$52,157
Intergovernmental Revenue	317,472	249,041	68,431
Charges for Services	203,183	231,169	(27,986)
Licenses and Permits	78,856	128,975	(50,119)
Investment Earnings	22,415	13,217	9,198
Fines and Forfeitures	10,173	11,643	(1,470)
All Other Revenue	17,636	19,222	(1,586)
Total	\$1,626,127	\$1,577,502	\$48,625

General Fund revenues in 2005 remained very stable, increasing approximately 3% compared to revenues in year 2004.

	2005 Expenditures	2004 Expenditures	Increase (Decrease)
Security of Persons and Property	\$1,037,820	\$1,041,889	(\$4,069)
Public Health and Welfare Services	45,069	56,424	(11,355)
General Government	560,311	488,485	71,826
Total	\$1,643,200	\$1,586,798	\$56,402

General Fund expenditures increased approximately 4% compared to 2004. Expenditures for general government increased nearly 15% due mainly to increases in costs of materials and supplies and utilities.

	2005 Other Financing Sources (Uses)	2004 Other Financing Sources (Uses)	Increase (Decrease)
Sale of Capital Assets	\$5,651	\$425	\$5,226
Transfers In	128,000	163,562	(35,562)
Transfers Out	(139,004)	(152,008)	13,004
Total	(\$5,353)	\$11,979	(\$17,332)

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2005***

Unaudited

FEMA Fund – The City's FEMA Fund balance decreased due to large amounts of grant monies being expended for flood reimbursement.

Electric Trust Fund – The City's Electric Trust Fund balance remained very stable, increasing by approximately 3%.

Capital Improvement Fund - The Capital Improvement Fund balance increased approximately 2%. This fund reported large increases in capital contributions to the wastewater fund for expenditures related to the phase five sanitary sewer project as well as loan proceeds for a bridge project.

The City's budget is prepared according to Ohio law and is based on accounting for certain transactions on a basis of cash receipts, disbursements and encumbrances. The most significant budgeted fund is the General Fund.

During the course of fiscal year 2005 the City amended its General Fund budget several times, none significant.

For the General Fund, budget basis revenue of \$1,575,776 did not significantly change from original budget estimates of \$1,585,848. The General Fund had an adequate fund balance to cover expenditures.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2005 the City had \$13,118,325 net of accumulated depreciation invested in land, buildings, equipment and vehicles. Of this total, \$3,709,581 was related to governmental activities and \$9,408,744 to the business-type activities. The following table shows fiscal year 2005 and 2004 balances:

	Governmental Activities		Increase (Decrease)
	2005	2004	
Land	\$298,749	\$175,335	\$123,414
Construction In Progress	170,763	5,150	165,613
Buildings	1,850,488	1,850,488	0
Improvements Other than Buildings	124,205	124,205	0
Machinery and Equipment	2,238,289	1,997,857	240,432
Infrastructure	988,032	154,879	833,153
Less: Accumulated Depreciation	(1,960,945)	(1,923,840)	(37,105)
Totals	<u>\$3,709,581</u>	<u>\$2,384,074</u>	<u>\$1,325,507</u>

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2005**

Unaudited

The primary increase occurred in infrastructure, which consisted of improvements to west north street as well as bike trail improvements.

	Business-Type Activities		Increase (Decrease)
	2005	2004	
Land	\$177,511	\$177,511	\$0
Construction in Progress	3,025,800	504,169	2,521,631
Buildings	1,973,207	1,973,207	0
Improvements Other than Buildings	450,250	450,250	0
Machinery and Equipment	1,293,461	1,326,634	(33,173)
Infrastructure	6,665,424	6,585,147	80,277
Less: Accumulated Depreciation	(4,176,909)	(3,876,973)	(299,936)
Totals	\$9,408,744	\$7,139,945	\$2,268,799

The primary increase occurred in construction in progress, which can be attributed to the phase five sanitary sewer construction project. Additional information on the City's capital assets can be found in Note 9.

Debt

At December 31, 2005, the City had \$3,885,000 in general obligation bonds outstanding, \$150,000 due within one year. The following table summarizes the City's debt outstanding as of December 31, 2005 and 2004:

	2005	2004
Governmental Activities:		
Ohio Public Works Commission Loan	\$5,143	\$0
West Street Bridge Project Loan	265,000	0
ODOT Street Improvement Loan	635,337	0
Capital Leases	118,599	121,824
Compensated Absences	223,645	152,047
Total Governmental Activities	1,247,724	273,871
Business-Type Activities:		
General Obligation Bonds	3,885,000	4,030,000
Ohio Public Works Commission Loans	535,745	13,140
Ohio Water Development Authority Loans	3,356,693	1,623,018
Compensated Absences	64,223	121,662
Total Business-Type Activities	7,841,661	5,787,820
Totals	\$9,089,385	\$6,061,691

Under current state statutes, the City's general obligation bonded debt issues are subject to a legal limitation based on 10.5% of the total assessed value of real and personal property. In addition, the unvoted net debt of municipal corporations cannot exceed 5.5% of the total assessed value of property. At December 31, 2005, the City's outstanding debt was below the legal limit. Additional information on the City's long-term debt can be found in Note 11.

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2005***

Unaudited

ECONOMIC FACTORS

At one time, the City of East Palestine was known for its pottery production with the potteries being the largest employers in the City. Currently the City has only one pottery left. A recycling company has purchased one of the closed potteries and the other one was torn down years ago. The City has five industrial plants with the remaining businesses being mainly sole-proprietor businesses. A fifty two lot housing development is under way, as well as a new development in the northwest area of town. New business development in the City in 2005 included a fresh meat market as well as some antique stores.

The City's 2006 budget is very conservative, with the exception of the FEMA Flood Prevention Project, which is near completion.

The City's school district has just completed two years of building additions and improvements. The school district is the City's largest withholding employer of City Income Tax.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, 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 Ms. Connie Robinson, Finance Director of the City of East Palestine.

This Page Intentionally Left Blank

CITY OF EAST PALESTINE, OHIO

Statement of Net Assets
December 31, 2005

	<u>Governmental</u> <u>Activities</u>	<u>Business-Type</u> <u>Activities</u>	<u>Total</u>
Assets:			
Cash and Cash Equivalents	\$ 492,258	\$ 91,535	\$ 583,793
Investments	150,000	0	150,000
Receivables:			
Taxes	535,984	0	535,984
Accounts	59,707	161,354	221,061
Intergovernmental	1,931,004	0	1,931,004
Interest	10,220	0	10,220
Special Assessments	841	0	841
Loans	17,164	0	17,164
Internal Balances	35,000	(35,000)	0
Inventory of Supplies at Cost	9,082	10,469	19,551
Prepaid Items	33,611	6,847	40,458
Capital Assets, Net	3,709,581	9,408,744	13,118,325
Total Assets	<u>6,984,452</u>	<u>9,643,949</u>	<u>16,628,401</u>
Liabilities:			
Accounts Payable	1,101,846	179,232	1,281,078
Accrued Wages and Benefits	130,740	30,565	161,305
Intergovernmental Payable	2,404	0	2,404
Deferred Revenue	358,850	0	358,850
Accrued Interest Payable	9,739	138,859	148,598
Noncurrent liabilities:			
Due within one year	104,764	287,605	392,369
Due in more than one year	1,142,960	7,554,056	8,697,016
Total Liabilities	<u>2,851,303</u>	<u>8,190,317</u>	<u>11,041,620</u>
Net Assets:			
Invested in Capital Assets, Net of Related Debt	2,685,502	1,918,058	4,603,560
Restricted For:			
Debt Service	21,184	0	21,184
Other Purposes	3,884,284	0	3,884,284
Unrestricted (Deficit)	(2,457,821)	(464,426)	(2,922,247)
Total Net Assets	<u>\$ 4,133,149</u>	<u>\$ 1,453,632</u>	<u>\$ 5,586,781</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Activities
For the Year Ended December 31, 2005

	Expenses	Program Revenues		
		Charges for Services and Sales	Operating Grants and Contributions	Capital Grants and Contributions
Governmental Activities:				
Security of Persons and Property	\$ 2,109,466	\$ 214,527	\$ 977,725	\$ 270,950
Leisure Time Activities	241,259	64,317	0	200,780
Community Environment	374,872	8,966	501,985	0
Public Health and Welfare	45,069	39,537	0	0
Transportation	364,062	0	278,365	0
General Government	719,460	56,609	0	268,147
Interest and Fiscal Charges	10,739	0	0	0
Total Governmental Activities	3,864,927	383,956	1,758,075	739,877
Business-Type Activities:				
Water	441,212	448,536	64,779	67,000
Wastewater	1,057,916	905,906	76,802	0
Total Business-Type Activities	1,499,128	1,354,442	141,581	67,000
Totals	\$ 5,364,055	\$ 1,738,398	\$ 1,899,656	\$ 806,877

General Revenues

- Property Taxes Levied for:
 - General Purposes
 - Special Purposes
- Income Tax
- Other Local Taxes
- Grants and Entitlements not Restricted to Specific Programs
- Investment Earnings
- Miscellaneous
- Transfers
- Total General Revenues and Transfers

- Change in Net Assets

- Net Assets Beginning of Year
- Net Assets End of Year

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Net (Expense) Revenue
and Changes in Net Assets

Governmental Activities	Business-Type Activities	Total
\$ (646,264)	\$ 0	\$ (646,264)
23,838	0	23,838
136,079	0	136,079
(5,532)	0	(5,532)
(85,697)	0	(85,697)
(394,704)	0	(394,704)
(10,739)	0	(10,739)
<u>(983,019)</u>	<u>0</u>	<u>(983,019)</u>
0	139,103	139,103
<u>0</u>	<u>(75,208)</u>	<u>(75,208)</u>
<u>0</u>	<u>63,895</u>	<u>63,895</u>
<u>(983,019)</u>	<u>63,895</u>	<u>(919,124)</u>
122,859	0	122,859
229,393	0	229,393
865,543	0	865,543
506	0	506
327,164	0	327,164
22,957	0	22,957
134,016	0	134,016
(7,958)	7,958	0
<u>1,694,480</u>	<u>7,958</u>	<u>1,702,438</u>
711,461	71,853	783,314
<u>3,421,688</u>	<u>1,381,779</u>	<u>4,803,467</u>
<u>\$ 4,133,149</u>	<u>\$ 1,453,632</u>	<u>\$ 5,586,781</u>

CITY OF EAST PALESTINE, OHIO

**Balance Sheet
Governmental Funds
December 31, 2005**

	General	FEMA	Electric Trust	Capital Improvement	Other Governmental Funds	Total Governmental Funds
Assets:						
Cash and Cash Equivalents	\$ 4,710	\$ 11,869	\$ 207,160	\$ 6,805	\$ 261,714	\$ 492,258
Investments	20,692	0	0	29,895	99,413	150,000
Receivables:						
Taxes	279,017	0	0	0	256,967	535,984
Accounts	59,642	0	0	0	65	59,707
Intergovernmental	238,213	798,017	0	243,682	651,092	1,931,004
Interest	9,514	0	0	0	706	10,220
Special Assessments	0	0	0	0	841	841
Loans	0	0	0	0	17,164	17,164
Interfund Loans Receivables	0	0	2,912,008	0	0	2,912,008
Inventory of Supplies, at Cost	0	0	0	0	9,082	9,082
Prepaid Items	32,370	0	0	0	1,241	33,611
Total Assets	\$ 644,158	\$ 809,886	\$ 3,119,168	\$ 280,382	\$ 1,298,285	\$ 6,151,879
Liabilities:						
Accounts Payable	\$ 23,801	\$ 810,006	\$ 0	\$ 256,438	\$ 11,601	\$ 1,101,846
Accrued Wages and Benefits Payable	106,204	0	0	0	24,536	130,740
Intergovernmental Payable	2,404	0	0	0	0	2,404
Interfund Loans Payable	780,000	0	0	2,009,962	87,046	2,877,008
Deferred Revenue	282,725	0	0	0	857,067	1,139,792
Total Liabilities	1,195,134	810,006	0	2,266,400	980,250	5,251,790
Fund Balance:						
Reserved for Encumbrances	9,629	0	0	4,287	127,582	141,498
Reserved for Prepaid Items	32,370	0	0	0	1,241	33,611
Reserved for Supplies Inventory	0	0	0	0	9,082	9,082
Reserved for Endowments	0	0	0	0	49,166	49,166
Undesignated, Unreserved in:						
General Fund (Deficit)	(592,975)	0	0	0	0	(592,975)
Special Revenue Funds (Deficit)	0	(120)	3,119,168	0	4,312	3,123,360
Debt Service Fund	0	0	0	0	20,343	20,343
Capital Project Funds (Deficit)	0	0	0	(1,990,305)	106,309	(1,883,996)
Total Fund Balance	(550,976)	(120)	3,119,168	(1,986,018)	318,035	900,089
Total Liabilities and Fund Balance	\$ 644,158	\$ 809,886	\$ 3,119,168	\$ 280,382	\$ 1,298,285	\$ 6,151,879

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

***Reconciliation Of Total Governmental Fund Balances
To Net Assets Of Governmental Activities
December 31, 2005***

Total Governmental Fund Balances	\$	900,089
<i>Amounts reported for governmental activities in the statement of net assets are different because</i>		
Capital Assets used in governmental activities are not resources and therefore are not reported in the funds.		3,709,581
Other long-term assets are not available to pay for current- period expenditures and therefore are deferred in the funds.		780,942
Long-term liabilities, including loans payable, are not due and payable in the current period and therefore are not reported in the funds.		
Compensated Absences Payable	(223,645)	
OPWC Loan Payable	(5,143)	
West Street Bridge Project Loan	(265,000)	
ODOT Loan	(635,337)	
Capital Leases	(118,599)	
Accrued Interest Payable	(9,739)	
	<u> </u>	<u>(1,257,463)</u>
<i>Net Assets of Governmental Activities</i>	\$	<u>4,133,149</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended December 31, 2005**

	General	FEMA	Electric Trust	Capital Improvement	Other Governmental Funds	Total Governmental Funds
Revenues:						
Taxes	\$ 976,392	\$ 0	\$ 0	\$ 0	\$ 224,673	\$ 1,201,065
Intergovernmental Revenues	317,472	928,303	0	493,391	845,406	2,584,572
Charges for Services	203,183	0	0	0	90,171	293,354
Licenses and Permits	78,856	0	0	0	0	78,856
Investment Earnings	22,415	0	0	0	542	22,957
Fines and Forfeitures	10,173	0	0	0	1,171	11,344
All Other Revenue	17,636	0	79,168	78	37,134	134,016
Total Revenue	1,626,127	928,303	79,168	493,469	1,199,097	4,326,164
Expenditures:						
Current:						
Security of Persons and Property	1,037,820	962,217	0	0	36,008	2,036,045
Public Health and Welfare	45,069	0	0	0	0	45,069
Leisure Time Activities	0	0	0	0	202,474	202,474
Community Environment	0	0	0	0	374,872	374,872
Transportation	0	0	0	0	319,428	319,428
General Government	560,311	0	0	0	48,237	608,548
Capital Outlay	0	0	0	3,621,353	488,095	4,109,448
Debt Service:						
Interest & Fiscal Charges	0	0	0	0	1,000	1,000
Total Expenditures	1,643,200	962,217	0	3,621,353	1,470,114	7,696,884
Excess (Deficiency) of Revenues						
Over (Under) Expenditures	(17,073)	(33,914)	79,168	(3,127,884)	(271,017)	(3,370,720)
Other Financing Sources (Uses):						
Sale of Capital Assets	5,651	0	0	0	0	5,651
Ohio Public Works Commission Loan	0	0	0	0	5,143	5,143
Ohio Department of Transportation Loan	0	0	0	635,337	0	635,337
Bridge Loan	0	0	0	0	265,000	265,000
Other Financing Sources - Capital Lease	0	0	0	55,817	0	55,817
Transfers In	128,000	0	0	2,482,004	52,899	2,662,903
Transfers Out	(139,004)	(399)	0	0	(9,827)	(149,230)
Total Other Financing Sources (Uses)	(5,353)	(399)	0	3,173,158	313,215	3,480,621
Net Change in Fund Balance	(22,426)	(34,313)	79,168	45,274	42,198	109,901
Fund Balance (Deficit) at Beginning of Year	(528,550)	34,193	3,040,000	(2,031,292)	274,374	788,725
Increase in Inventory Reserve	0	0	0	0	1,463	1,463
Fund Balance (Deficit) End of Year	\$ (550,976)	\$ (120)	\$ 3,119,168	\$ (1,986,018)	\$ 318,035	\$ 900,089

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

***Reconciliation Of The Statement Of Revenues, Expenditures
And Changes In Fund Balances Of Governmental Funds
To The Statement Of Activities
For The Fiscal Year Ended December 31, 2005***

Net Change in Fund Balances - Total Governmental Funds		\$ 109,901
<i>Amounts reported for governmental activities in the statement of activities are different because</i>		
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		
Capital Outlay	1,538,453	
Depreciation Expense	<u>(177,614)</u>	1,360,839
The statement of activities reports losses arising from the disposal of capital assets. Conversely, the governmental funds do not report any loss on the disposal of capital assets.		
		(35,332)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.		
		258,182
The issuance of long-term debt (e.g. notes, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of government funds. Neither transaction, however, has any effect on net assets.		
OPWC Loan	(5,143)	
West Street Bridge Project Loan	(265,000)	
ODOT Loan	(635,337)	
New Capital Lease	<u>(55,817)</u>	(961,297)
Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.		
Capital Lease Payment		59,042
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds.		
Compensated Absences	(71,598)	
Change in Inventory	<u>1,463</u>	(70,135)
In the statement of activities, interest is accrued on outstanding debt, whereas in governmental funds, an interest expenditure is reported when due.		
		<u>(9,739)</u>
<i>Change in Net Assets of Governmental Activities</i>		<u>\$ 711,461</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, 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, 2005**

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)
Revenues:				
Taxes	\$ 989,650	\$ 994,980	\$ 983,365	\$ (11,615)
Intergovernmental Revenue	263,173	264,591	261,502	(3,089)
Charges for Services	204,482	205,583	203,183	(2,400)
Licenses and Permits	76,825	77,239	76,337	(902)
Investment Earnings	21,083	21,196	20,949	(247)
Fines and Forfeitures	10,836	10,894	10,767	(127)
All Other Revenues	19,799	19,905	19,673	(232)
Total Revenues	<u>1,585,848</u>	<u>1,594,388</u>	<u>1,575,776</u>	<u>(18,612)</u>
Expenditures:				
Current:				
Security of Persons and Property	1,054,238	1,071,706	1,052,232	19,474
Public Health and Welfare	44,855	45,599	44,770	829
General Government	547,196	556,263	546,155	10,108
Total Expenditures	<u>1,646,289</u>	<u>1,673,568</u>	<u>1,643,157</u>	<u>30,411</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	(60,441)	(79,180)	(67,381)	11,799
Other Financing Sources (Uses):				
Sale of Capital Assets	5,651	5,651	5,651	0
Transfers In	128,000	128,000	128,000	0
Transfers Out	(139,004)	(139,004)	(139,004)	0
Advances In	70,000	70,000	70,000	0
Total Other Financing Sources (Uses):	<u>64,647</u>	<u>64,647</u>	<u>64,647</u>	<u>0</u>
Net Change in Fund Balance	4,206	(14,533)	(2,734)	11,799
Fund Balance at Beginning of Year	7,108	7,108	7,108	0
Prior Year Encumbrances	10,251	10,251	10,251	0
Fund Balance at End of Year	<u>\$ 21,565</u>	<u>\$ 2,826</u>	<u>\$ 14,625</u>	<u>\$ 11,799</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in
Fund Balance – Budget and Actual (Non-GAAP Budgetary Basis)
Special Revenue Fund - FEMA Fund
For the Year Ended December 31, 2005**

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)
Revenues:				
Intergovernmental Revenue	\$ 2,000,000	\$ 200,744	\$ 196,484	\$ (4,260)
Total Revenues	2,000,000	200,744	196,484	(4,260)
Expenditures:				
Current:				
Security of Persons and Property	2,000,000	200,345	195,744	4,601
Total Expenditures	2,000,000	200,345	195,744	4,601
Excess (Deficiency) of Revenues Over (Under) Expenditures	0	399	740	341
Other Financing Sources (Uses):				
Transfers Out	0	(399)	(399)	0
Total Other Financing Sources (Uses):	0	(399)	(399)	0
Net Change in Fund Balance	0	0	341	341
Fund Balance at Beginning of Year	11,528	11,528	11,528	0
Fund Balance at End of Year	\$ 11,528	\$ 11,528	\$ 11,869	\$ 341

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in
Fund Balance – Budget and Actual (Non-GAAP Budgetary Basis)
Special Revenue Fund - Electric Trust Fund
For the Year Ended December 31, 2005**

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)
Revenues:				
All Other Revenues	\$ 100,000	\$ 100,000	\$ 79,168	\$ (20,832)
Total Revenues	100,000	100,000	79,168	(20,832)
Expenditures:				
Total Expenditures	0	0	0	0
Excess (Deficiency) of Revenues Over (Under) Expenditures	100,000	100,000	79,168	(20,832)
Other Financing Sources (Uses):				
Advances Out	0	(105,000)	(105,000)	0
Total Other Financing Sources (Uses):	0	(105,000)	(105,000)	0
Net Change in Fund Balance	100,000	(5,000)	(25,832)	(20,832)
Fund Balance at Beginning of Year	232,992	232,992	232,992	0
Fund Balance at End of Year	\$ 332,992	\$ 227,992	\$ 207,160	\$ (20,832)

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Net Assets
Proprietary Funds
December 31, 2005

	Business-Type Activities		
	Enterprise Funds		
	Water	Wastewater	Total
ASSETS			
Current assets:			
Cash and Cash Equivalents	\$ 74,157	\$ 17,378	\$ 91,535
Receivables:			
Accounts	52,360	108,994	161,354
Inventory of Supplies at Cost	9,385	1,084	10,469
Prepaid Items	3,261	3,586	6,847
Total current assets	<u>139,163</u>	<u>131,042</u>	<u>270,205</u>
Noncurrent assets:			
Capital Assets, Net	1,176,429	8,232,315	9,408,744
Total noncurrent assets	<u>1,176,429</u>	<u>8,232,315</u>	<u>9,408,744</u>
Total assets	<u>1,315,592</u>	<u>8,363,357</u>	<u>9,678,949</u>
LIABILITIES			
Current liabilities:			
Accounts Payable	41,307	137,925	179,232
Accrued Wages and Benefits	10,856	19,709	30,565
Accrued Interest Payable	10,632	128,227	138,859
General Obligation Bonds Payable - Current	6,615	143,385	150,000
OWDA Loans Payable - Current	41,525	56,230	97,755
OPWC Loans Payable - Current	2,920	26,950	29,870
Total Current Liabilities	<u>113,855</u>	<u>512,426</u>	<u>626,281</u>
Noncurrent Liabilities:			
General Obligation Bonds Payable	105,480	3,629,520	3,735,000
OWDA Loans Payable	249,146	3,009,792	3,258,938
OPWC Loans Payable	7,300	498,575	505,875
Interfund Loan Payable	10,000	25,000	35,000
Compensated Absences Payable	37,080	27,143	64,223
Total noncurrent liabilities	<u>409,006</u>	<u>7,190,030</u>	<u>7,599,036</u>
Total Liabilities	<u>522,861</u>	<u>7,702,456</u>	<u>8,225,317</u>
NET ASSETS			
Invested in Capital Assets, Net of Related Debt	763,443	1,154,615	1,918,058
Unrestricted	29,288	(493,714)	(464,426)
Total Net Assets	<u>\$ 792,731</u>	<u>\$ 660,901</u>	<u>\$ 1,453,632</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended December 31, 2005

	Business-Type Activities		
	Enterprise Funds		
	Water	Wastewater	Total
Operating Revenues:			
Charges for Services	\$ 447,902	\$ 903,719	\$ 1,351,621
Total Operating Revenues	447,902	903,719	1,351,621
Operating Expenses:			
Personal Services	151,189	293,952	445,141
Contractual Services	59,141	158,388	217,529
Materials and Supplies	61,917	22,845	84,762
Utilities	52,530	119,307	171,837
Depreciation	80,876	253,284	334,160
Total Operating Expenses	405,653	847,776	1,253,429
Operating Income	42,249	55,943	98,192
Non-Operating Revenue (Expenses):			
Interest and Fiscal Charges	(35,354)	(209,674)	(245,028)
Operating Grants	64,779	76,802	141,581
Capital Contributions	67,000	2,521,631	2,588,631
Other Nonoperating Revenue	634	2,187	2,821
Other Nonoperating Expense	(205)	(466)	(671)
Total Non-Operating Revenues (Expenses)	96,854	2,390,480	2,487,334
Income Before Transfers	139,103	2,446,423	2,585,526
Transfers:			
Transfers-In	0	18,681	18,681
Transfers-Out	(98,508)	(2,433,846)	(2,532,354)
Total Transfers	(98,508)	(2,415,165)	(2,513,673)
Change in Net Assets	40,595	31,258	71,853
Net Assets Beginning of Year	752,136	629,643	1,381,779
Net Assets End of Year	\$ 792,731	\$ 660,901	\$ 1,453,632

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2005

	Business-Type Activities		Totals
	Enterprise Funds		
	Water	Wastewater	
<u>Cash Flows from Operating Activities:</u>			
Cash Received from Customers	\$449,965	\$908,736	\$1,358,701
Cash Payments for Goods and Services	(134,311)	(187,320)	(321,631)
Cash Payments to Employees	(148,545)	(358,019)	(506,564)
Net Cash Provided by Operating Activities	167,109	363,397	530,506
<u>Cash Flows from Noncapital Financing Activities:</u>			
Advances In from Other Funds	10,000	25,000	35,000
Transfers Out to Other Funds	(81,827)	(2,433,846)	(2,515,673)
Net Cash Used by Noncapital Financing Activities	(71,827)	(2,408,846)	(2,480,673)
<u>Cash Flows from Capital and Related Financing Activities:</u>			
Acquisition and Construction of Assets	(1,250)	(5,552)	(6,802)
Proceeds from Ohio Water Development Authority Loan	0	1,830,213	1,830,213
Proceeds from Ohio Public Works Commission Loan	0	539,000	539,000
Principal Paid on General Obligation Bond	(15,000)	(128,000)	(143,000)
Principal Paid on Ohio Public Works Commission Loan	(2,920)	(13,475)	(16,395)
Interest Paid on All Debt	(13,760)	(190,113)	(203,873)
Net Cash Provided (Used) by Capital and Related Financing Activities	(32,930)	2,032,073	1,999,143
Net Increase (Decrease) in Cash and Cash Equivalents	62,352	(13,376)	48,976
Cash and Cash Equivalents at Beginning of Year	11,805	30,754	42,559
Cash and Cash Equivalents at End of Year	\$74,157	\$17,378	\$91,535
<u>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</u>			
Operating Income	\$42,249	\$55,943	\$98,192
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:			
Depreciation Expense	80,876	253,284	334,160
Miscellaneous Nonoperating Revenue	634	2,187	2,821
Miscellaneous Nonoperating Expense	(205)	(466)	(671)
Changes in Assets and Liabilities:			
Decrease in Accounts Receivable	1,429	2,830	4,259
Decrease in Inventory	4,740	255	4,995
Increase in Prepaid Items	(1,456)	(954)	(2,410)
Increase (Decrease) in Accounts Payable	36,405	119,761	156,166
Increase (Decrease) in Accrued Wages and Benefits	74	(3,948)	(3,874)
Decrease in Intergovernmental Payable	(232)	(5,461)	(5,693)
Increase (Decrease) in Compensated Absences	2,595	(60,034)	(57,439)
Total Adjustments	124,860	307,454	432,314
Net Cash Provided by Operating Activities	\$167,109	\$363,397	\$530,506

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Assets and Liabilities
Fiduciary Funds
December 31, 2005

	<u>Agency Fund</u>
Assets:	
Cash and Cash Equivalents	\$ 321
Total Assets	<u>321</u>
Liabilities:	
Due to Others	<u>321</u>
Total Liabilities	<u>321</u>
Total Net Assets	<u><u>\$ 0</u></u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of East Palestine, Ohio (the "City") is a home rule municipal corporation created under the laws of the State of Ohio. East Palestine was first incorporated as a village on February 27, 1876. The City currently operates under and is governed by its own Charter. The current Charter, which provides for a Council-City Manager form of government, was adopted in 1990.

The accompanying basic financial statements comply with the provisions of Governmental Accounting Standards Board (the "GASB") Statement No. 14, *"The Financial Reporting Entity,"* in that the financial statements include all organizations, activities, functions and component units for which the City (the reporting entity) is financially accountable. Financial accountability is defined as the appointment of a voting majority of a legally separate organization's governing body and either the City's ability to impose its will over the organization, or the possibility that the organization will provide a financial benefit to or impose a financial burden on the City. There were no potential component units that met the criteria imposed by GASB Statement No. 14 to be included in the City's reporting entity. Based on the foregoing, the reporting entity of the City includes the following services: police and fire protection, emergency medical, parks, recreation, planning, zoning, street maintenance and other governmental services. In addition, the City owns and operates a water treatment and distribution system and a wastewater treatment and collection system, which are reported as enterprise funds.

The accounting policies and financial reporting practices of the City conform to generally accepted accounting principles as applicable to governmental units. The following is a summary of its significant accounting policies:

B. Basis of Presentation - Fund Accounting

The accounting system is organized and operated on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures (expenses). The various funds are summarized by type in the basic financial statements. The following fund types are used by the City:

Governmental Funds - The governmental funds are those funds through which most governmental functions are typically financed. The acquisition, use and balances of the City's expendable financial resources and the related current liabilities (except those accounted for in the proprietary funds) are accounted for through governmental funds. The measurement focus is upon determination of "financial flow" (sources, uses and balances of financial resources). The following are the City's major governmental funds:

General Fund - This fund is used to account for all financial resources except those resources accounted for in another fund. The general fund balance is available to the City for any purpose provided it is expended or transferred according to the general laws of Ohio and the provisions of the City Charter.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Basis of Presentation - Fund Accounting (Continued)

FEMA Fund - This fund is used to account for federal monies awarded in response to storm damages.

Electric Trust Fund - This fund was created to account for proceeds received by the City from the sale of the City Electric Plant. These proceeds may be used by the City for purposes approved by city council.

Capital Improvement Fund - This fund is used to account for the financial resources used for the major capital projects undertaken by the City.

Proprietary Funds - The proprietary funds are accounted for on an "economic resources" measurement focus. This measurement focus provides that all assets and liabilities associated with the operation of the proprietary funds are included on the balance sheet. The proprietary fund operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

Enterprise Funds - These funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. The City's major enterprise funds are:

Water Fund - This fund is used to account for the operation of the City's water service.

Wastewater Fund - This fund is used to account for the operation of the City's sanitary sewer service.

Fiduciary Funds - Trust and Agency Funds - These funds are used to account for assets held by a government unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units and/or other funds. The City maintains one agency fund. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.

C. Basis of Presentation - Financial Statements

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 statements distinguish between those activities of the City that are governmental and those that are considered business-type activities.

The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of the proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Basis of Presentation – Financial Statements (Continued)

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function or program of the City's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of 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 function is self-financing or draws from the general revenues of the City.

Fund Financial Statements – Fund financial statements report detailed information about the City. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. Fiduciary funds are reported by fund type.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental fund types are accounted for using a flow of current financial resources measurement focus. The financial statements for governmental funds are a balance sheet, which generally includes only current assets and current liabilities, and a statement of revenues, expenditures and changes in fund balances, which reports on the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources.

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

D. Basis of Accounting

Basis of accounting represents the methodology utilized in the recognition of revenues and expenditures or expenses reported in the financial statements. The accounting and reporting treatment applied to a fund is determined by its measurement focus.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Basis of Accounting (Continued)

The modified accrual basis of accounting is followed by the governmental funds. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual, i.e., both measurable and available. The term "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period, which for the City is 60 days after year end. Expenditures are recognized in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on general long-term debt which is recognized when due.

Non-exchange transactions, in which the City receives value without directly giving equal value in return, include income taxes, property taxes, grants, entitlements and donations. Revenue from income taxes is recognized in the period in which the income is earned and is available. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied and the revenue is available. 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 specific purpose, and expenditure requirements, in which the resources are provided to the City on a reimbursement basis.

Revenues considered susceptible to accrual at year end include income taxes withheld by employers, interest on investments, special assessments and state levied locally shared taxes (including motor vehicle license fees and local government assistance). Other revenues, including licenses, permits, certain charges for services, income taxes other than those withheld by employers and miscellaneous revenues, are recorded as revenues when received in cash because generally these revenues are not measurable until received.

Property taxes measurable as of December 31, 2005 but which are not intended to finance 2005 operations and delinquent property taxes, whose availability is indeterminate, are recorded as deferred revenue as further described in Note 5.

The accrual basis of accounting is utilized for reporting purposes by the government-wide statements, proprietary funds and agency funds. Revenues are recognized when earned and expenses are recognized when they are incurred.

Pursuant to GASB Statement No. 20, *"Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting,"* the City follows GASB guidance as applicable to proprietary funds and FASB Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements. The City has elected not to apply FASB statements and interpretations issued after November 30, 1989 to its business-type activities and enterprise funds.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process

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 appropriation ordinance, all of which are prepared on the budgetary basis of accounting. The certificate of estimated resources and the appropriation ordinance are subject to amendment throughout the year.

All funds other than agency funds are legally required to be budgeted and appropriated; however, only governmental funds are required to be reported. The primary level of budgetary control is at the object level within each department. Budgetary modifications may only be made by ordinance of the City Council.

1. Tax Budget

By July 15, the City Manager submits an annual tax budget for the following fiscal year 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.

2. Estimated Resources

The County Budget Commission reviews estimated revenue and determines if the budget substantiates a need to levy all or part of previously authorized taxes. The Budget Commission then certifies its actions to the City by September 1 of each year. As part of the certification process, the City receives an official certificate of estimated resources stating the projected receipts by 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 do 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 any unencumbered fund balances from the preceding year. The certificate may be further amended during the year if a new source of revenue is identified or actual receipts exceed current estimates. The amounts reported on the budgetary statement reflect the amounts in the final amended official certificate of estimated resources issued during 2005.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process (Continued)

3. Appropriations

A temporary appropriation ordinance to control expenditures may be passed on or about January 1 of each year for the period January 1 through March 31. An annual appropriation ordinance must be passed by April 1 of each year for the period January 1 through December 31. The appropriation ordinance establishes spending controls at the fund, department and object level. The appropriation ordinance may be amended during the year as additional information becomes available, provided that total fund appropriations do not exceed the current estimated resources as certified. The allocation of appropriations among departments and objects within a fund may be modified during the year by an ordinance of City Council. During 2005, several supplemental appropriations were necessary to budget the use of contingency funds. Administrative control is maintained through the establishment of more detailed line-item budgets. The budgetary figures which appear in the "Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual - for the General and Major Special Revenue Funds" are provided on the budgetary basis to provide a comparison of actual results to the final budget, including all amendments and modifications.

4. Encumbrances

As part of formal budgetary control, purchase orders, contracts and other commitments for expenditures are encumbered and recorded as the equivalent of expenditures (budget basis) in order to reserve that portion of the applicable appropriation and to determine and maintain legal compliance. However, on the GAAP basis of accounting, encumbrances do not constitute expenditures or liabilities and are reported as reservations of fund balances for governmental funds in the accompanying basic financial statements.

5. Lapsing of Appropriations

At the close of each fiscal year, the unencumbered balance of each appropriation reverts to the respective fund from which it was appropriated and becomes subject to future appropriations. The encumbered appropriation balance is carried forward to the subsequent fiscal year and need not be reappropriated.

6. Budgetary Basis of Accounting

The City's budgetary process accounts for certain transactions on a basis other than generally accepted accounting principles (GAAP). The major differences between the budgetary basis and the GAAP basis lie in the manner in which revenues and expenditures are recorded. Under the budgetary basis, revenues and expenditures are recognized on a cash basis. Utilizing the cash basis, revenues are recorded when received in cash and expenditures when paid. Under the GAAP basis, revenues and expenditures are recorded on the modified accrual basis of accounting.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process (Continued)

6. Budgetary Basis of Accounting (Continued)

The following table summarizes the adjustments necessary to reconcile the GAAP basis statements to the budgetary basis statements for the General and Major Special Revenue funds:

	Net Change in Fund Balances		
	General Fund	FEMA Fund	Electric Trust Fund
GAAP Basis (as reported)	(\$22,426)	(\$34,313)	\$79,168
Increase (Decrease):			
Accrued Revenues at December 31, 2005 received during 2006	(233,661)	(798,017)	(2,912,008)
Accrued Revenues at December 31, 2004 received during 2005	253,310	66,198	2,807,008
Accrued Expenditures at December 31, 2005 paid during 2006	132,409	810,006	0
Accrued Expenditures at December 31, 2004 paid during 2005	(120,652)	(43,533)	0
2004 Prepays for 2005	31,433	0	0
2005 Prepays for 2006	(32,370)	0	0
Outstanding Encumbrances	(10,777)	0	0
Budget Basis	<u>(\$2,734)</u>	<u>\$341</u>	<u>(\$25,832)</u>

F. Cash and Cash Equivalents

Cash and cash equivalents include amounts in demand deposits, the State Treasurer's Asset Reserve (STAR Ohio), repurchase agreements and certificates of deposit. The repurchase agreements and STAR Ohio are considered cash equivalents because of their highly liquid nature.

The City pools a majority of its cash for investment and resource management purposes. Each fund's equity in pooled cash and investments represents the balance on hand as if each fund maintained its own cash and investment account. For purposes of the statement of cash flows, the proprietary funds' shares of equity in pooled repurchase agreements and certificates of deposit are considered to be cash equivalents. See Note 4, "Cash, Cash Equivalents and Investments."

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

G. Investments

Investment procedures and interest allocations are restricted by provisions of the Ohio Constitution and the Ohio Revised Code. In accordance with GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools", the City reports its investments at fair value, except for nonparticipating investment contracts (certificates of deposit and repurchase agreements) which are reported at cost.

The City has invested funds in the STAR Ohio during 2005. 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, 2005. See Note 4, "Cash, Cash Equivalents and Investments."

H. Inventory

Inventory is stated at cost (first-in, first-out) in the governmental funds and at the lower of cost or market in the proprietary funds. The costs of inventory items are recorded as expenditures in the governmental funds when purchased and as expenses in the proprietary funds when used.

I. Capital Assets and Depreciation

Capital assets are defined by the City as assets with an initial, individual cost of more than \$1,000.

1. Property, Plant and Equipment - Governmental Activities

Governmental activities capital assets are those not directly related to the business type funds. These generally are acquired or constructed for governmental activities and are recorded as expenditures in the governmental funds and are capitalized at cost (or estimated historical cost for assets not purchased in recent years). These assets are reported in the Governmental Activities column of the Government-wide Statement of Net Assets, but they are not reported in the Fund Financial Statements.

Contributed capital assets are recorded at fair market value at the date received. Capital assets include land, buildings, building improvements, machinery, equipment and infrastructure. Infrastructure is defined as long-lived capital assets that normally are stationary in nature and normally can be preserved for a significant number of years. Examples of infrastructure include roads, bridges, curbs and gutters, streets and sidewalks, drainage systems and lighting systems.

Estimated historical costs for governmental activities capital asset values were initially determined by identifying historical costs when such information was available. In cases where information supporting original cost was not obtainable, estimated historical costs were developed. For certain capital assets, the estimates were arrived at by indexing estimated current costs back to the estimated year of acquisition.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

I. Capital Assets and Depreciation (Continued)

2. Property, Plant and Equipment – Business Type Activities

Property, plant and equipment acquired by the proprietary funds are stated at cost (or estimated historical cost), including interest capitalized during construction and architectural and engineering fees where applicable. Contributed capital assets are recorded at fair market value at the date received. These assets are reported in both the Business-Type Activities column of the Government-wide Statement of Net Assets and in the respective funds.

3. Depreciation

All capital assets are depreciated, excluding land and construction in progress. Depreciation has been provided using the straight-line method over the following estimated useful lives:

Description	Governmental and Business-Type Activities Estimated Lives (in years)
Buildings	30 - 40
Improvements other than Buildings	50
Machinery, Equipment, Furniture and Fixtures	5 - 15
Infrastructure	50 - 100

J. Long-Term Obligations

Long-term liabilities are being repaid from the following funds:

Obligation	Fund
Ohio Water Development Authority Loans	Water Fund Wastewater Fund
General Obligation Bond	Wastewater Fund
Ohio Public Works Commission Loan	General Bond Retirement Fund Water Fund, Wastewater Fund
Compensated Absences	General Fund Street Construction, Maintenance and Repair Fund Water Fund, Wastewater Fund
West Street Bridget Project Loan	Bridge Fund
Ohio Department of Transportation Loan	Street Construction, Maintenance and Repair Fund
Capital Leases	General Fund, Capital Improvement Fund

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

K. Compensated Absences

In accordance with GASB Statement No. 16, "Accounting for Compensated Absences," vacation and compensatory time are accrued as liabilities when an employee's right to receive compensation is attributable to services already rendered and it is probable that the employee will be compensated through paid time off or some other means, such as cash payments at termination or retirement. Leave time that has been earned but is unavailable for use as paid time off or as some other form of compensation because an employee has not met the minimum service time requirement, is accrued to the extent that it is considered to be probable that the conditions for compensation will be met in the future.

Sick leave is accrued using the vesting method, whereby the liability is recorded on the basis of leave accumulated by employees who are eligible to receive termination payments as of the balance sheet date, and on leave balances accumulated by other employees who are expected to become eligible in the future to receive such payments.

For governmental funds, that portion of unpaid compensated absences that is expected to be paid using expendable, available resources is reported as an expenditure in the fund from which the individual earning the leave is paid, and a corresponding liability is reflected in the account "Compensated Absences Payable." In the government wide statement of net assets, "Compensated Absences Payable" is recorded within the "Due within one year" account and the long-term portion of the liability is recorded within the "Due in more than one year" account.

Compensated absences are expensed in the Water and Wastewater Funds when earned, and the related liability is reported within the fund.

L. 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 borrowings used for the acquisition, construction of 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.

M. Pensions

The provision for pension costs is recorded when the related payroll is accrued and the obligation is incurred.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

N. Interfund Activity

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 financial statements.

O. Reservations of Fund Balance

Reserves indicate that a portion of fund balance is not available for expenditure or is legally segregated for a specific future use. Fund balances are reserved for supplies inventory, prepaid items, endowments and encumbered amounts which have not been accrued at year end.

P. Operating Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items. 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 water treatment and distribution and wastewater collection and treatment. Operating expenses are necessary costs incurred to provide the goods or services that are the primary activity of the fund. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Q. 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 the City and that are either unusual in nature or infrequent in occurrence. The City had no extraordinary or special items to report during fiscal year 2005.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 2 – RESTATEMENT OF FUND BALANCE/NET ASSETS

Certain adjustments were made to the Governmental Activities and Business-Type Activities net asset beginning balance due to errors in accounting for Ohio Water Development Authority Loans and accumulated depreciation on capital assets. As a result of the restatement, the City's Governmental Activities net assets at December 31, 2004 decreased \$532,799, to a restated amount of \$3,421,688. The Business-Type Activities net assets at December 31, 2004 decreased \$286,752 to a restated amount of \$1,381,779.

NOTE 3 - COMPLIANCE AND ACCOUNTABILITY

Fund Deficits - The fund deficits at December 31, 2005 of \$550,976 in the General Fund, \$120 in the FEMA Fund, \$86,474 in the Downtown Revitalization Fund (special revenue funds) and \$1,986,018 in the Capital Improvement Fund (capital projects fund) arise from the recognition of expenditures on the modified accrual basis which are greater than expenditures recognized on the budgetary/cash basis. The general fund provides transfers when cash is required, not when accruals occur.

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS

Cash resources of several individual funds are combined to form a pool of cash, cash equivalents and investments. In addition, investments are separately held by a number of individual funds. Statutes require the classification of funds held by the City into three categories:

Category 1 consists of "active" funds - those funds required to be kept in "cash" or "near cash" status for immediate use by the City. Such funds must be maintained either as cash in the City Treasury or in depository accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts.

Category 2 consists of "inactive" funds - those funds not required for use within the current five year period of designation of depositories. Inactive funds may be deposited or invested only as certificates of deposit maturing no later than the end of the current period of designation of depositories.

Category 3 consists of "interim" funds - those funds not needed for immediate use but needed before the end of the current period of designation of depositories. Interim funds may be invested or deposited in the following securities:

- 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;

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

- 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;
- 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;
- Interim deposits in eligible institutions applying for interim funds;
- Bonds and other obligations of the State of Ohio;
- No-load money market mutual funds consisting exclusively of obligations described in the first two bullets of this section and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions, and
- The State Treasury Asset Reserve of Ohio (STAR Ohio).

A. Deposits

Custodial credit risk is the risk that in the event of bank failure, the government's deposits may not be returned. Protection of City cash and deposits is provided by the federal deposit insurance corporation as well as qualified securities pledged by the institution holding the assets. Ohio Law requires that deposits be placed in eligible banks or savings and loan associations located in Ohio. Any public depository in which the City places deposits must pledge as collateral eligible securities of aggregate market value equal to the excess of deposits not insured by the Federal Deposit Insurance Corporation (FDIC). The securities pledged as collateral are pledged to a pool for each individual financial institution in amounts equal to at least 105% of the carrying value of all public deposits held by each institution. Obligations that may be pledged as collateral are limited to obligations of the United States and its agencies and obligations of any state, county, municipal corporation or other legally constituted authority of any other state, or any instrumentality of such county, municipal corporation or other authority. Collateral is held by trustees including the Federal Reserve Bank and designated third party trustees of the financial institutions.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

A. Deposits (Continued)

At year end the carrying amount of the City's deposits was \$198,754 and the bank balance was \$233,485. Federal depository insurance covered \$136,041 of the bank balance and \$97,444 was uninsured. Of the remaining uninsured bank balance, the City was exposed to custodial risk as follows:

	<u>Balance</u>
Uninsured and collateralized with securities held by the pledging institution's trust department not in the City's name	\$97,444
Total Balance	\$97,444

Investment earnings of \$23,191 earned by other funds were credited to the General Fund as required by state statute.

B. Investments

The City's investments at December 31, 2005 are summarized below:

	<u>Fair Value</u>	<u>Credit Rating</u>	<u>Investment Maturities (in Years)</u>		
			<u>less than 1</u>	<u>1-3</u>	<u>3-5</u>
STAR Ohio	\$213,830	AAAm ¹	\$213,830	\$0	\$0
Repurchase Agreement	321,530	N/A	321,530	0	0
Total Investments	\$535,360		\$535,360	\$0	\$0

¹ Standard & Poor's

Interest Rate Risk – The Ohio Revised Code generally limits security purchases to those that mature within five years of settlement date.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

C. Reconciliation of Cash, Cash Equivalents and Investments

The classification of cash, cash equivalents and investments on the financial statements is based on criteria set forth in GASB Statement No. 9. STAR Ohio and certificates of deposit with an original maturity of three months or less are treated as cash equivalents. The classification of cash and cash equivalents (deposits) for purposes of this note are based on criteria set forth in GASB Statement No. 3.

	<u>Cash and Cash Equivalents</u>	<u>Investments</u>
Per Balance Sheet	\$584,114	\$150,000
Certificates of Deposit (with maturities of more than 3 months)	150,000	(150,000)
Investments:		
STAR Ohio	(213,830)	213,830
Repurchase Agreement	<u>(321,530)</u>	<u>321,530</u>
Per GASB Statement No. 3	<u><u>\$198,754</u></u>	<u><u>\$535,360</u></u>

NOTE 5 - PROPERTY TAXES

Property taxes include amounts levied against all real estate and public utility property, and tangible personal property used in business and located in the City. Real property taxes (other than public utility) collected during 2005 were levied after October 1, 2004 on assessed values as of January 1, 2004 the lien date. Assessed values were established by the County Auditor at 35 percent of appraised market value. All property is required to be revalued every six years. The last revaluation was completed in 2004. Real property taxes are payable annually or semi-annually. The first payment is due January 20; the remainder is payable by June 20.

Taxes collected from tangible personal property (other than public utility) in one calendar year are levied in the prior calendar year on assessed values during and at the close of the most recent fiscal year of the taxpayer that ended on or before March 31 of that calendar year, and at the 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 of the year assessed. Single county taxpayers may pay annually or semi-annually. The first payment is due April 30; the remainder is payable by September 20.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 5 - PROPERTY TAXES (Continued)

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 is currently assessed at 100 percent of its 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 East Palestine. The County Auditor periodically remits to the City its portion of the taxes collected.

The full property tax rate for all City operations for the year ended December 31, 2005 was \$6.90 per \$1,000 of assessed value. The assessed value upon which the 2005 tax receipts was based was \$63,048,940. This amount constitutes \$55,987,580 in real property assessed value, \$2,791,330 in public utility assessed value, and \$4,270,030 in tangible personal property assessed value.

Ohio law prohibits taxation of property from all taxing authorities in excess of 1% of assessed value without a vote of the people. Under current procedures, the City's share is .69% (6.9 mills) of assessed value.

The City levies a tax of 1.0% on all salaries, wages, commissions and other compensation, on net profits earned within the City and on incomes of residents earned outside the City. Employers within the City are required to withhold income tax on employee compensation and remit the tax to the City either monthly or quarterly, as required. Corporations and other individual taxpayers are required to pay their estimated tax quarterly and file a declaration annually.

NOTE 6 - RECEIVABLES

Receivables at December 31, 2005 consisted of taxes, interest, accounts receivable, CDBG loans, special assessments, interfund receivables and intergovernmental receivables.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 7 - TRANSFERS

Following is a summary of transfers in and out for all funds for 2005:

Fund	Transfer In	Transfer Out
General Fund	\$128,000	\$139,004
FEMA Fund	0	399
Capital Improvement Fund	2,482,004	0
Other Governmental Funds	52,899	9,827
Total Governmental Funds	2,662,903	149,230
Water Fund	0	98,508
Wastewater Fund	18,681	2,433,846
Total Proprietary Funds	18,681	2,532,354
Totals	<u>\$2,681,584</u>	<u>\$2,681,584</u>

NOTE 8 - INTERFUND RECEIVABLES AND PAYABLES

The following is a summary of interfund loans receivable and payable for all funds for 2005:

Fund	Interfund Loans Receivable	Interfund Loans Payable
General Fund	\$0	\$780,000
Electric Trust Fund	2,912,008	0
Capital Improvement Fund	0	2,009,962
Other Governmental Funds	0	87,046
Water Fund	0	10,000
Wastewater Fund	0	25,000
Totals	<u>\$2,912,008</u>	<u>\$2,912,008</u>

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 9 - CAPITAL ASSETS

A. Governmental Activities Capital Assets

Summary by category of changes in governmental activities capital assets at December 31, 2005:

<i>Historical Cost:</i>	Restated			December 31,
Class	December 31,	Additions	Deletions	2005
	2004			
<i>Capital assets not being depreciated:</i>				
Land	\$175,335	\$123,414	\$0	\$298,749
Construction in Progress	5,150	170,763	(5,150)	170,763
Subtotal	180,485	294,177	(5,150)	469,512
<i>Capital assets being depreciated:</i>				
Buildings	1,850,488	0	0	1,850,488
Improvements Other than Buildings	124,205	0	0	124,205
Machinery and Equipment	1,997,857	411,123	(170,691)	2,238,289
Infrastructure	154,879	833,153	0	988,032
Subtotal	4,127,429	1,244,276	(170,691)	5,201,014
Total Cost	<u>\$4,307,914</u>	<u>\$1,538,453</u>	<u>(\$175,841)</u>	<u>\$5,670,526</u>
<i>Accumulated Depreciation:</i>				
Class	Restated			December 31,
	December 31,	Additions	Deletions	2005
	2004			
Buildings	(\$527,666)	(\$37,551)	\$0	(\$565,217)
Improvements Other than Buildings	(21,715)	(5,589)	0	(27,304)
Machinery and Equipment	(1,370,973)	(115,961)	140,509	(1,346,425)
Infrastructure	(3,486)	(18,513)	0	(21,999)
Total Depreciation	<u>(\$1,923,840)</u>	<u>(\$177,614) *</u>	<u>\$140,509</u>	<u>(\$1,960,945)</u>
<i>Net Value:</i>	<u>\$2,384,074</u>			<u>\$3,709,581</u>

* Depreciation expenses were charged to governmental functions as follows:

Security of Persons and Property	\$70,008
Leisure Time Activities	38,650
Transportation	44,458
General Government	24,498
Total Depreciation Expense	<u>\$177,614</u>

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 9 - CAPITAL ASSETS (Continued)

B. Business-Type Activities Capital Assets

Summary by Category at December 31, 2005:

Historical Cost:

Class	December 31, 2004	Additions	Deletions	December 31, 2005
<i>Capital assets not being depreciated:</i>				
Land	\$177,511	\$0	\$0	\$177,511
Construction in Progress	504,169	2,521,631	0	3,025,800
Subtotal	<u>681,680</u>	<u>2,521,631</u>	<u>0</u>	<u>3,203,311</u>
<i>Capital assets being depreciated:</i>				
Buildings	1,973,207	0	0	1,973,207
Improvements Other than Buildings	450,250	0	0	450,250
Machinery and Equipment	1,326,634	1,051	(34,224)	1,293,461
Infrastructure	6,585,147	80,277	0	6,665,424
Subtotal	<u>10,335,238</u>	<u>81,328</u>	<u>(34,224)</u>	<u>10,382,342</u>
Total Cost	<u>\$11,016,918</u>	<u>\$2,602,959</u>	<u>(\$34,224)</u>	<u>\$13,585,653</u>

Accumulated Depreciation:

Class	December 31, 2004	Additions	Deletions	December 31, 2005
Buildings	(\$1,035,085)	(\$49,330)	\$0	(\$1,084,415)
Improvements Other than Buildings	(235,759)	(8,785)	0	(244,544)
Machinery and Equipment	(803,335)	(122,756)	34,224	(891,867)
Infrastructure	(1,802,794)	(153,289)	0	(1,956,083)
Total Depreciation	<u>(\$3,876,973)</u>	<u>(\$334,160)</u>	<u>\$34,224</u>	<u>(\$4,176,909)</u>

Net Value:

	<u>\$7,139,945</u>	<u>\$9,408,744</u>
--	--------------------	--------------------

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 10 – DEFINED BENEFIT PENSION PLANS

All of the City's full-time employees participate in one of two separate retirement systems which are cost-sharing multiple employer defined benefit pension plans.

A. Ohio Public Employees Retirement System (the "Ohio PERS")

The following information was provided by the Ohio PERS to assist the City in complying with GASB Statement No. 27, "Accounting for Pensions by State and Local Government Employers."

All employees of the City, except full-time uniformed police officers and full-time firefighters, participate in one of the three pension plans administered by the Ohio PERS: the Traditional Pension Plan (TP), the Member-Directed Plan (MD), and the Combined Plan (CO). The TP Plan is a cost-sharing multiple employer defined benefit pension plan. The MD 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 MD Plan members accumulate retirement assets equal to the value of member and (vested) employer contributions plus any investment earnings thereon. The CO Plan is a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. Under the CO Plan employer contributions are invested by the retirement system to provide a formula retirement benefit similar in nature to the TP Plan. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the MD Plan.

The Ohio PERS provides retirement, disability, survivor and death benefits and annual cost-of-living adjustments to members of the TP Plan and CO Plan. Members of the MD Plan do not qualify for ancillary benefits, including postemployment health care benefits. Chapter 145 of the Ohio Revised Code provides statutory authority to establish and amend benefits. The Ohio Public Employees Retirement System issues a stand-alone financial report that includes financial statements and required supplementary information for the Ohio PERS. Interested parties may obtain a copy by making a written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 222-6701 or 1-800-222-7377.

The Ohio Revised Code provides statutory authority for employee and employer contributions. For 2005, employee and employer contribution rates were consistent across all three plans (TP, MD and CO). The employee contribution rate is 8.5%. The 2005 employer contribution rate for local government employer units was 13.55%, of covered payroll, 9.55% to fund the pension and 4.0% to fund health care. The contribution requirements of plan members and the City are established and may be amended by the Public Employees Retirement Board. The City's contributions to the Ohio PERS for the years ending December 31, 2005, 2004, and 2003 were \$157,023, \$149,520, and \$149,228, respectively, which were equal to the required contributions for each year.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 10 – DEFINED BENEFIT PENSION PLANS (Continued)

A. Ohio Public Employees Retirement System (the “Ohio PERS”) (Continued)

The Ohio PERS provides postemployment health care benefits to age and service retirants with ten or more years of qualifying Ohio service credit under the TP and CO plans and to primary survivor recipients of such retirants. Health care coverage for disability recipients is also available. The health care coverage provided by the Ohio PERS is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. A portion of each employer's contribution to the Ohio PERS is set aside for the funding of post retirement health care. The Ohio Revised Code provides statutory authority requiring public employers to fund postemployment health care through their contributions to the Ohio PERS. The portion of the 2005 employer contribution rate (identified above) that was used to fund health care for the year 2005 was 4.0% of covered payroll which amounted to \$46,354.

The significant actuarial assumptions and calculations relating to postemployment health care benefits were based on the Ohio Public Employees Retirement System's latest actuarial review performed as of December 31, 2004. An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability. All investments are carried at market value. For actuarial valuation purposes, a smoothed market approach is used. Under this approach assets are adjusted annually to reflect 25% of unrealized market appreciation or depreciation on investment assets. The investment assumption rate for 2004 was 8.0%. An annual increase of 4.0% compounded annually, is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases, over and above the 4.0% base increase, were assumed to range from 0.5% to 6.3%. Health care costs were assumed to increase 4.0% annually plus an additional factor ranging from 1% to 6% for the next 8 years. In subsequent years (9 and beyond) health care costs were assumed to increase 4% (the projected wage inflation rate).

Benefits are advanced-funded on an actuarially determined basis. The number of active contributing participants for the TP and CO Plans was 376,109. The actuarial value of the Ohio PERS net assets available for OPEB at December 31, 2004 is \$10.8 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$29.5 billion and \$18.7 billion, respectively.

The Health Care Preservation Plan (HCPP) adopted by the OPERS Retirement Board on September 9, 2004, will be effective January 1, 2007. In addition to the HCPP, Ohio PERS has taken additional action to improve the solvency of the Health Care Fund in 2005 by creating a separate investment pool for health care assets. As an additional component of the HCPP, member and employer contribution rates increased as of January 1, 2006, which will allow additional funds to be allocated to the health care plan

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 10 – DEFINED BENEFIT PENSION PLANS (Continued)

B. Ohio Police and Fire Pension Fund (the “OP&F Fund”)

All City full-time police officers and full-time firefighters participate in the OP&F Fund, a cost-sharing multiple-employer defined benefit pension plan. The OP&F Fund provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries. Contribution requirements and benefit provisions are established by the Ohio State Legislature and are codified in Chapter 742 of the Ohio Revised Code. The Ohio Police and Fire Pension Fund issues a stand-alone financial report that includes financial statements and required supplementary information for the OP&F Fund. Interested parties may obtain a copy by making a written request to 140 East Town Street, Columbus, Ohio 43215-5164 or by calling (614) 228-2975.

Plan members are required to contribute 10.0% of their annual covered salary, while employers are required to contribute 19.5% and 24.0% respectively for police officers and firefighters. The City's contributions to the OP&F Fund for the years ending December 31, 2005, 2004, and 2003 were \$54,962, \$56,184 and \$57,685 for police and \$12,105, \$11,319 and \$10,982 for firefighters, respectively, which were equal to the required contributions for each year.

The OP&F Fund provides postemployment health care coverage to any person who received or is eligible to receive a monthly 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 on a full-time or two-thirds basis. The health care coverage provided by the OP&F Fund is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. The Ohio Revised Code provides that health care costs paid from the funds of the OP&F Fund shall be included in the employer's contribution rate. The Ohio Revised Code also provides statutory authority allowing the Fund's Board of Trustees to provide postemployment health care coverage to all eligible individuals from the employer's contributions to the OP&F Fund.

The portion of the 2005 covered payroll that was used to fund postemployment health care benefits was \$21,844 representing 7.75% of covered payroll for police and \$3,909 representing 7.75% of covered payroll for fire. Health care funding and accounting was on a pay-as-you-go basis. 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. As of December 31, 2004, the date of the last actuarial evaluation available, the number of participants eligible to receive health care benefits was 13,812 for police and 10,528 for firefighters. The OP&F Fund does not provide separate data on the funded status and funding progress of postemployment health care benefits. The Fund's total health care expenses for the year ended December 31, 2004 were \$102,173,796, which was net of member contributions of \$55,665,341.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 11 - LONG-TERM OBLIGATIONS

Long-term debt and other long-term obligations of the City at December 31, 2005 were as follows:

		Restated Balance December 31, 2004	Additions	Deductions	Balance December 31, 2005	Amount Due Within One Year
Governmental Activities:						
Ohio Public Works Commission Loan:						
Bridge Replacement	2005	\$0	\$5,143	\$0	\$5,143	\$0
West Street Bridge Project Loan	2005	0	265,000	0	265,000	0
Ohio Department of Transportation						
Street Improvement Loan	2005	0	635,337	0	635,337	0
Capital Leases		121,824	55,817	(59,042)	118,599	57,943
Compensated Absences Payable		152,047	223,645	(152,047)	223,645	46,821
Total Governmental Activities		<u>273,871</u>	<u>1,184,942</u>	<u>(211,089)</u>	<u>1,247,724</u>	<u>104,764</u>
Business-Type Activities:						
General Obligation Bonds:						
Various Purpose Bond	1999	1,885,000	0	(100,000)	1,785,000	105,000
Sewerage System Refunding Bond	2003	2,145,000	0	(45,000)	2,100,000	45,000
Total General Obligation Bonds:		<u>4,030,000</u>	<u>0</u>	<u>(145,000)</u>	<u>3,885,000</u>	<u>150,000</u>
Ohio Public Works Commission Loan:						
Waterline Improvement	2000	13,140	0	(2,920)	10,220	2,920
Phase Five Sanitary Sewer	2005	0	539,000	(13,475)	525,525	26,950
Total OPWC Loans:		<u>13,140</u>	<u>539,000</u>	<u>(16,395)</u>	<u>535,745</u>	<u>29,870</u>
Ohio Water Development Authority Loans:						
Water Treatment Plant	1992	332,196	0	(41,525)	290,671	41,525
Sewer Project - Phase Two	1999	1,004,070	0	(55,013)	949,057	56,230
Wastewater Treatment Plant	2004	286,752	1,830,213	0	2,116,965	0
Total OWDA Loans:		<u>1,623,018</u>	<u>1,830,213</u>	<u>(96,538)</u>	<u>3,356,693</u>	<u>97,755</u>
Compensated Absences		121,662	64,223	(121,662)	64,223	9,980
Total Business-Type Activities		<u>5,787,820</u>	<u>2,433,436</u>	<u>(379,595)</u>	<u>7,841,661</u>	<u>287,605</u>
Totals		<u>\$6,061,691</u>	<u>\$3,618,378</u>	<u>(\$590,684)</u>	<u>\$9,089,385</u>	<u>\$392,369</u>

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 11 - LONG-TERM OBLIGATIONS (Continued)

A. Principal and Interest Requirements

A summary of the City's future long-term debt funding requirements, including principal and interest payments as of December 31, 2005, follows:

Years	OPWC Loan		West Street Bridge Loan		ODOT Loan	
	Principal	Interest	Principal	Interest	Principal	Interest
2006	\$29,870	\$0	\$0	\$11,687	\$0	\$0
2007	35,013	0	0	11,687	0	0
2008	29,870	0	265,000	11,687	55,315	18,304
2009	28,410	0	0	0	56,997	16,621
2010	26,950	0	0	0	58,731	14,888
2011-2015	134,750	0	0	0	321,561	46,531
2016-2020	134,750	0	0	0	142,733	4,503
2021-2025	121,275	0	0	0	0	0
2026-2031	0	0	0	0	0	0
Totals	<u>\$540,888</u>	<u>\$0</u>	<u>\$265,000</u>	<u>\$35,061</u>	<u>\$635,337</u>	<u>\$100,847</u>

Years	General Obligation Bond		OWDA Loans		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2006	\$150,000	\$199,760	\$97,755	\$40,920	\$277,625	\$252,367
2007	150,000	193,678	195,099	57,498	380,112	262,863
2008	160,000	187,595	197,334	52,356	707,519	269,942
2009	165,000	178,480	199,609	47,172	450,016	242,273
2010	55,000	102,980	201,923	41,953	342,604	159,821
2011-2015	985,000	748,375	921,141	138,787	2,362,452	933,693
2016-2020	1,055,000	478,500	863,746	66,011	2,196,229	549,014
2021-2025	505,000	276,150	563,887	20,259	1,190,162	296,409
2026-2031	660,000	117,850	116,199	630	776,199	118,480
Totals	<u>\$3,885,000</u>	<u>\$2,483,368</u>	<u>\$3,356,693</u>	<u>\$465,586</u>	<u>\$8,682,918</u>	<u>\$3,084,862</u>

B. Ohio Water Development Authority Loans

In 2004, the City entered into an agreement with the OWDA, as administrator for the U. S. Environmental Protection Agency (EPA), for the City to receive a loan of \$2,400,000. The amount is subject to change and has not been finalized. The interest rate on the loan is 1.00%, per annum. This loan is payable from wastewater charges and is received by the City in increments as the project is completed. As of December 31, 2005, the City had received \$2,116,965 from OWDA. Subsequent amounts will be received in future years. An estimate of future financing requirements has been made based on the \$2,116,965 loan balance at December 31, 2005.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2005**

NOTE 11 - LONG-TERM OBLIGATIONS (Continued)

C. Defeased Debt

In February 2003, the City defeased \$2,236,000 of FHA Loans for Sewer Improvements through the issuance of \$2,235,000 of General Obligation Bonds for Sewer System Improvements. The net proceeds of the 2003 Bonds have been invested in obligations guaranteed as to both principal and interest by the United States and placed in irrevocable escrow accounts which, including interest earned, will be used to pay the principal and interest on the refunded bonds. The refunded bonds, which have an outstanding balance of \$2,134,000 at December 31, 2005, are not included in the City's outstanding debt since the City has in-substance satisfied its obligations through the advance refunding. The refunding was undertaken to reduce total debt service payments over the next 26 years by \$363,369 and resulted in an economic gain of \$205,434. The acquisition price exceeded the net carrying amount of the old debt by \$30,054.

NOTE 12 - CAPITAL LEASES

The City leases several pieces of equipment under capital leases. The original cost of the equipment and the related liability are reported on the Government – wide Statement of Net Assets.

The following is a schedule of future minimum lease payments under the capital lease together with the present value of the net minimum lease payments as of December 31, 2005:

<u>Year Ending December 31,</u>	<u>Capital Leases</u>
2006	\$62,979
2007	27,918
2008	12,643
2009	12,643
2010	12,643
Minimum Lease Payments	<u>128,826</u>
Less amount representing interest at the City's incremental borrowing rate of interest	<u>(10,227)</u>
Present value of minimum lease payments	<u>\$118,599</u>

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2005

NOTE 13 - INSURANCE AND RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The City is a participant in the Public Entities Pool of Ohio (the "Pool"). The Pool was established in 1987 and is administered under contract by American Risk Pooling Consultants Inc. to provide a program of property and casualty insurance for its member organizations throughout the State of Ohio.

The Pool's general objectives are to formulate, develop and administer a program of insurance, to obtain lower costs for that coverage, and to develop a comprehensive loss control program on behalf of the member political subdivisions. Political subdivisions joining the Pool may withdraw at the end of any coverage period upon 60 days prior written notice to the Pool. Under agreement, members who terminate participation in the Pool as well as current members are subject to a supplemental assessment or a refund, at the discretion of the Board of Trustees, depending on the ultimate loss experience of all the entities it insures for each coverage year. To date, there has been no assessments or refunds, due to the limited period of time that the Pool has been in existence and the nature of the coverage that is afforded to the participants.

The City of East Palestine obtained insurance coverage from the Pool for the years 2000 through 2006 for losses related to general liability, public officials liability, automobile, law enforcement liability, medical malpractice liability, and employee benefits liability.

Each participant makes an annual "contribution" to the Pool for the coverage they are provided, based on rates established by the Pool, using anticipated and actual results of operation for the various coverages provided. Participants are also charged for a "surplus contribution" that is used to build the Pool's retained earning account to fund the activities of the Pool. During 2005, the City of East Palestine made contributions to the Pool totaling \$79,438.

In the ordinary course of business, the Pool cedes a portion of its exposure to other insurers. These arrangements limit the Pool's maximum net loss on individual risks.

Treaty basis casualty excess of loss contracts in force at December 31, 2005 generally protect the Pool against individual losses over \$250,000.

Losses exceeding \$250,000 are reinsured with American Public Entity Excess Pool (APEEP) in an amount not to exceed \$2,000,000 per claim and \$5,000,000 in aggregate per year.

The Pool is, and ultimately the participants are, contingently liable should any reinsurer become unable to meet its obligations under the reinsurance agreements.

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 coverages in any of the past three fiscal years.

Worker's Compensation claims are covered through the City's participation in the State of Ohio's program. The City pays the State Worker's Compensation System a premium based upon a rate per \$100 of payroll. The rate is determined based on accident history and administrative costs.

CITY OF EAST PALESTINE, OHIO

***Notes to the Basic Financial Statements
For the Year Ended December 31, 2005***

NOTE 14 - CONTINGENCIES

The City is a party to various legal proceedings which seek damages or injunctive relief generally incidental to its operations and pending projects. The City's management is of the opinion that the ultimate disposition of various claims and legal proceedings will not have a material effect, if any, on the financial condition of the City.

NOTE 15 - CONSTRUCTION COMMITMENTS

The City had the following contractual commitments at December 31, 2005:

<u>Project</u>	<u>Remaining Contractual Commitment</u>	<u>Expected Date of Completion</u>
Phase V - WWTP Improvements	\$221,723	2006
Leslie Run Creek Restoration Project	476,224	2006
West Street Bridge Improvements	123,351	2007
Flood Damage - Sewer Plant	556,195	2006

**WOLFE, WILSON, & PHILLIPS, INC.
37 SOUTH SEVENTH STREET
ZANESVILLE, OHIO 43701**

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

City of East Palestine
Columbiana County
82 Garfield Avenue
East Palestine, Ohio 44413

We have audited the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of East Palestine as of and for the year ended December 31, 2005, which collectively comprise the City's basic financial statements and have issued our report thereon dated January 5, 2007. 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 City of East Palestine's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of East Palestine'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 no instances of noncompliance or other matters that we must report under *Government Auditing Standard*. We noted certain immaterial instances of noncompliance, which we have reported to management of City of East Palestine in a separate letter dated January 5, 2007.

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

Wolfe, Wilson, & Phillips, Inc.
Zanesville, Ohio
January 5, 2007

**WOLFE, WILSON, & PHILLIPS, INC.
37 SOUTH SEVENTH STREET
ZANESVILLE, OHIO 43701**

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

City of East Palestine
Columbiana County
82 Garfield Avenue
East Palestine, Ohio 44413

Compliance

We have audited the compliance of City of East Palestine with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended December 31, 2005. City of East Palestine's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of City of East Palestine management. Our responsibility is to express an opinion on City of East Palestine's compliance based on our audit.

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

In our opinion, the City of East Palestine complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2005.

Internal Control Over Compliance

The management of City of East Palestine is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with *OMB Circular A-133*.

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

Page 2

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

Wolfe, Wilson, & Phillips, Inc.
Zanesville, Ohio
January 5, 2007

**CITY OF EAST PALESTINE
COLUMBIANA COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
OMB CIRCULAR A-133 SECTION 505**

1. Summary of Auditor's Results

(d)(1)(I)	Type of Financial Statement Opinion	Unqualified
(d)(1)(ii)	Were there any material control weakness conditions reported at the financial statement level (GAGAS)?	NO
(d)(1)(ii)	Were there any other reportable control weakness conditions reported at the financial statement level (GAGAS)?	NO
(d)(1)(iii)	Was there any reported non-compliance at the financial statement level (GAGAS)?	No
(d)(1)(iv)	Were there any material internal control weakness conditions reported for major federal programs?	NO
(d)(1)(iv)	Were there any other reportable internal control weakness conditions reported for major federal programs?	NO
(d)(1)(v)	Type of Major Programs' Compliance Opinion	Unqualified
(d)(1)(vi)	Are there any reportable findings under section. 510?	NO
(d)(1)(vii)	Major Programs:	Assistance to Firefighters; CFDA # 97.044 Disaster Assistance Grant; CFDA # 97.036
(d)(1)(viii)	Dollar Threshold: Type A/B Programs:	Type A: >\$300,000; Type B: All Others
(d)(1)(ix)	Low Risk Auditee?	No

2. Findings Related to the Financial Statements Required to be Reported in Accordance with GAGAS

NONE

3. Findings and Questioned Costs for Federal Awards

NONE

**CITY OF EAST PALESTINE
COLUMBIANA COUNTY
SCHEDULE OF FEDERAL AWARDS EXPENDITURES
FOR THE YEAR ENDED DECEMBER 31, 2005**

Federal Grantor/ Sub-Grantor Program Title	Pass Through Entity Number	Federal CFDA Number	Receipts	Non-Cash Receipts	Disbursements	Non-Cash Disbursements
<u>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:</u>						
(pass through Ohio Department of Development)						
Community Development Block Grant	A-C-03-116-1	14.228	\$ 45,575	\$ -	\$ 56,568	\$ -
	A-C-05-116-1		9,800	-	9,800	-
			<u>55,375</u>	<u>-</u>	<u>66,368</u>	<u>-</u>
HOME Investment Partnership Program	A-C-05-116-2	14.239	229,069	-	292,028	-
	A-C-03-116-2		6,500	-	6,500	-
			<u>235,569</u>	<u>-</u>	<u>298,528</u>	<u>-</u>
Total U.S. Department of Housing and Urban Development			290,944	-	364,896	-
<u>U.S. DEPARTMENT OF HOMELAND SECURITY:</u>						
Direct Award						
Assistance to Firefighters Grant Program	EMW-05-FG-19060	97.044	266,950	-	266,950	-
Disaster Assistance Grant (FEMA)	FEMA-DR-1519-OH	97.036	189,359	-	205,585	-
			<u>456,309</u>	<u>-</u>	<u>472,535</u>	<u>-</u>
Total U.S. Department of Homeland Security			456,309	-	472,535	-
Total Federal Awards Expenditures			<u>\$ 747,253</u>	<u>\$ -</u>	<u>\$ 837,431</u>	<u>\$ -</u>

See notes to Schedule of Federal Awards Expenditures.

**CITY OF EAST PALESTINE
NOTES TO SCHEDULE OF FEDERAL AWARDS EXPENDITURES**

NOTES A – SIGNIFICANT ACCOUNTING POLICIES

The accompanying schedule of federal awards expenditures is a summary of the activity of the City's federal award programs. The schedule has been prepared on the cash basis of accounting.

NOTE B - MATCHING REQUIREMENTS

Certain Federal programs require the City contribute non-Federal funds (matching funds) to support the Federally-funded programs. The City has complied with the matching requirements. The expenditure of non-Federal matching funds is not included on the Schedule.



Mary Taylor, CPA
Auditor of State

CITY OF EAST PALESTINE

COLUMBIANA 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
JUNE 19, 2007**