

**CITY OF HAMILTON! OHIO
GAS SYSTEM**

Financial Statements

Year Ended December 31, 2002

With

Independent Auditors' Report



**Auditor of State
Betty Montgomery**

Mayor and Members of Council
City of Hamilton!
345 High Street
Hamilton, Ohio 45011

We have reviewed the Independent Auditor's Report of the City of Hamilton! Ohio – Gas System, Butler County, prepared by Clark, Schaefer, Hackett & Co., for the audit period January 1, 2002 to December 31, 2002. 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 Hamilton! Ohio – Gas System is responsible for compliance with these laws and regulations.

A handwritten signature in cursive script that reads "Betty Montgomery".

BETTY MONTGOMERY
Auditor of State

August 4, 2003

This Page is Intentionally Left Blank.

CITY OF HAMILTON! OHIO – GAS SYSTEM

Table of Contents

| | <u>Page</u> |
|-----------------------------------------------------------|-------------|
| Independent Auditors' Report | 1 |
| Financial Statements: | |
| Statement of Financial Position | 2 |
| Statement of Revenues, Expenses and Changes in Net Assets | 3 |
| Statement of Cash Flows | 4 |
| Notes to Financial Statements | 5 - 11 |



Clark, Schaefer, Hackett & Co.
CERTIFIED PUBLIC ACCOUNTANTS
BUSINESS CONSULTANTS

INDEPENDENT AUDITORS' REPORT

Honorable City Council
City of Hamilton! Ohio

We have audited the accompanying financial statements of the City of Hamilton! Ohio - Gas System, an enterprise fund of the City of Hamilton! Ohio as of and for the year ended December 31, 2002, as listed in the table of contents. These financial statements are the responsibility of the City of Hamilton!'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As discussed in Note 1, the financial statements present only the Gas System and do not purport to, and do not, present fairly the financial position of the City of Hamilton! Ohio as of December 31, 2002, and the changes in its financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Hamilton! Ohio - Gas System as of December 31, 2002 and the changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1 to the financial statements, the Gas System adopted the provisions of Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – Management's Discussion and Analysis – For State and Local Governments*; Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*; Statement No. 38, *Certain Financial Statement Note Disclosures*; and Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*, as of January 1, 2002. This results in a change to the Gas System's format and content of the financial statements.

Clark, Schaefer, Hackett & Co.

Cincinnati, Ohio
June 16, 2003

CITY OF HAMILTON! OHIO – GAS SYSTEM
STATEMENT OF NET ASSETS
DECEMBER 31, 2002

ASSETS

Current assets:

| | |
|--------------------------------------------------------------------------------|------------------|
| Cash and cash equivalents | \$ 1,622,473 |
| Investments | 2,316,432 |
| Accounts receivable (less allowance for uncollectible accounts of \$2,578,234) | 4,684,485 |
| Interest receivable | 43,927 |
| Due from other funds | 5,000 |
| Inventory of supplies at cost | 113,950 |
| Prepaid expenses | <u>96,356</u> |
| Total current assets | <u>8,882,623</u> |

Restricted assets:

| | |
|---------------------------|------------------|
| Cash and cash equivalents | 2,525,420 |
| Investments | <u>1,054,125</u> |
| Total restricted assets | <u>3,579,545</u> |

Bond issuance costs

236,884

Capital assets:

| | |
|-------------------------------|---------------------|
| Property, plant and equipment | 57,368,740 |
| Construction in progress | 878,938 |
| Accumulated depreciation | <u>(19,800,042)</u> |
| Total capital assets | <u>38,447,636</u> |

Total assets

\$ 51,146,688

LIABILITIES

Current liabilities:

| | |
|-----------------------------------------|------------------|
| Accounts payable | \$ 2,503,877 |
| Accrued wages and benefits | 51,738 |
| Intergovernmental payable | 15,070 |
| Accrued interest payable | 159,469 |
| Revenue bonds payable - current portion | <u>695,000</u> |
| Total current liabilities | <u>3,425,154</u> |

Non-current liabilities:

| | |
|------------------------------|-------------------|
| Customer deposits payable | 399,770 |
| Compensated absences payable | 371,056 |
| Revenue bonds payable | <u>15,076,292</u> |
| Total noncurrent liabilities | <u>15,847,118</u> |

Total liabilities

19,272,272

NET ASSETS

| | |
|-------------------------------------------------|----------------------|
| Invested in capital assets, net of related debt | 22,676,344 |
| Unrestricted | <u>9,198,072</u> |
| Total net assets | \$ <u>31,874,416</u> |

See notes to financial statements.

CITY OF HAMILTON! OHIO - GAS SYSTEM
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEAR ENDED DECEMBER 31, 2002

| | |
|-------------------------------------------|----------------------|
| Operating revenues: | |
| Charges for services | \$ 21,917,517 |
| Other operating revenues | <u>3,956</u> |
| Total operating revenues | <u>21,921,473</u> |
| | |
| Operating expenses: | |
| Purchased gas | 15,058,714 |
| Personal services | 1,153,226 |
| Contractual services | 758,890 |
| Depreciation | 1,771,187 |
| Materials and supplies | 89,192 |
| Other operating expenses | <u>1,918,960</u> |
| Total operating expenses | <u>20,750,169</u> |
| | |
| Operating income | 1,171,304 |
| | |
| Non-operating revenues (expenses): | |
| Investment earnings | 218,252 |
| Loss on disposal of capital assets | (47,357) |
| Interest and fiscal charges | <u>(876,809)</u> |
| Total non-operating revenues (expenses) | <u>(705,914)</u> |
| | |
| Change in net assets | 465,390 |
| | |
| Net assets - beginning of year | <u>31,409,026</u> |
| | |
| Net assets - end of year | \$ <u>31,874,416</u> |

See notes to financial statements.

CITY OF HAMILTON! OHIO - GAS SYSTEM
STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2002

| | |
|------------------------------------------------------------------|---------------------|
| Cash flows from operating activities: | |
| Cash received from customers | \$ 21,217,641 |
| Cash paid for employee services and benefits | (1,195,935) |
| Cash paid to suppliers for goods and services | (18,068,864) |
| Other operating revenues | <u>4,578</u> |
| Net cash provided by operating activities | <u>1,957,420</u> |
| Cash flows from capital and related financing activities: | |
| Acquisition and construction of capital assets | (1,112,723) |
| Principal payment on debt | (670,000) |
| Interest payment on debt | <u>(824,313)</u> |
| Net cash used in capital and related financing activities | <u>(2,607,036)</u> |
| Cash flows from investing activities: | |
| Purchase of investments | (3,370,557) |
| Sale of investments | 5,949,326 |
| Interest from investments | <u>284,738</u> |
| Net cash provided by investing activities | <u>2,863,507</u> |
| Net change in cash and cash equivalents | 2,213,891 |
| Cash and cash equivalents at beginning of year | <u>1,934,002</u> |
| Cash and cash equivalents at end of year | \$ <u>4,147,893</u> |

Reconciliation of operating income to net cash provided by operating activities:

| | |
|-----------------------------------------------------------------------------------------|---------------------|
| Operating income | \$ 1,171,304 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | |
| Depreciation | 1,771,187 |
| Changes in assets and liabilities: | |
| Accounts receivable | (699,254) |
| Inventories | 7,160 |
| Prepaid expenses | (16,664) |
| Accrued wages and benefits | 11,888 |
| Intergovernmental payables | 8,856 |
| Accounts payable | 9,514 |
| Compensated absences payable | 15,351 |
| Customer deposits | 8,088 |
| Due to other funds | <u>(330,010)</u> |
| Net cash provided by operating activities | \$ <u>1,957,420</u> |

See notes to financial statements.

CITY OF HAMILTON! OHIO – GAS SYSTEM

Notes to Financial Statements Year Ended December 31, 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity – The City of Hamilton! Ohio – Gas System (Gas System) is a utility operating as a separate enterprise fund of the City of Hamilton! Ohio (City). The Gas System is controlled by and is dependent on the City's executive and legislative branches. Control by or dependence on the City is determined on the basis of outstanding debt secured by revenues or general obligations of the City, obligation of the City to finance any deficits that may occur, or receipt of subsidies from the City.

Measurement Focus, Basis of Accounting and Basis of Presentation – The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows. The Gas System has elected only to apply Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements.

Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Gas System's principal ongoing operations. The principal operating revenues are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses.

Income Taxes – The Gas System, which is owned and operated by the City, is exempt from income taxes since it is a division of a municipality.

Cash and Investments – Certain Gas System cash and investments are held in the City Treasury and pooled for investment management purposes. The portion of these pooled funds owned by the Gas System is reported as either cash and cash equivalents or investments, as appropriate. The Gas System's investments are stated at fair value. Interest earned on funds invested is distributed on the basis of the relationship of the average monthly balance of all funds, including the Gas System. The Gas System considers all highly liquid investments with a maturity of three months or less when purchased to be cash and cash equivalents.

Inventories – Inventories are stated at the lower of cost or market based on a moving-average cost method.

Capital Assets – Expenditures that increase values or extend the useful life of the respective assets are capitalized while the costs of maintenance and repairs are charged to operating expenses. Interest costs related to the construction of property, plant and equipment are capitalized. Depreciation is calculated on a straight-line basis over the estimated useful life of the various classes of assets. The range of useful lives for computing depreciation is 3 to 75 years.

Bond Discounts and Issuance Costs – Unamortized bond discounts and issuance costs are amortized on the interest method over the term of the related bonds. Amortization of bond discounts and issuance costs amounted to \$44,302 and \$20,835, respectively, in 2002.

Compensated Absences - The Gas System follows the provisions of GASB Statement No. 16, “Accounting for Compensated Absences”. Vacation and compensatory time benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the Gas System will compensate the employees for the benefits through paid time off or some other means. Sick leave termination benefits are accrued using the vesting method. The liability includes the employees who are currently eligible to receive termination benefits and those employees for whom it is probable that they will become eligible to receive payment in the future. The amount is based on accumulated sick leave and employees' wage rates at year-end.

Changes in Accounting Principles – For 2002, the Gas System implemented the following:

- GASB Statement No. 34 “*Basic Financial Statements and Management’s Discussion and Analysis for State and Local Governments.*”
- GASB Statement No. 37 “*Basic Financial Statements and Management’s Discussion and Analysis for State and Local Governments: Omnibus.*”
- GASB Statement No. 38 “*Certain Financial Statement Note Disclosure*”.
- GASB Interpretation No. 6 “*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.*”

GASB Statements no. 34, 37, and 38 create and amend new basic financial statements and note disclosure for reporting on the Gas System’s financial activities. These changes had no effect on prior year net assets.

Use of Estimates – The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. CASH AND INVESTMENTS

The Gas System follows the practice of pooling cash and investments with the City Treasurer except for the cash and investments of certain accounts maintained by trustees. Pooled cash and investments of the Gas System totaled \$3,938,905 at December 31, 2002 and consisted of demand deposits, money market funds, U.S. government securities and STAR Ohio.

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, 2002.

Deposits – The carrying amount of the Gas System’s deposits at December 31, 2002 was \$2,458,546 and the bank balance was \$2,557,305. Of the bank balance, \$120,912 was covered by federal depository insurance. The remaining amounts are considered uninsured and uncollateralized as defined by GASB Statement No. 3. However, the State of Ohio has established by statute a collateral pooling system for financial institutions acting as public depositories. Public depositories must pledge qualified securities with fair values greater than the total amount of all public deposits to be secured by the collateral pool. This pooled collateral covers the Gas System’s uninsured and uncollateralized deposits.

Investments – The State of Ohio statutes, Gas Revenue Bond indentures, and the City Charter authorize the City to invest in obligations of the U.S. Treasury, agencies, instrumentalities, and repurchase agreements. The Gas System’s investments are categorized as either (1) insured or registered, or securities held by the City or its agent in the City’s name; or (2) uninsured and unregistered, with securities held by the counterparty’s trust department or agent in the City’s name; or (3) uninsured and unregistered with securities held by the counterparty or its trust department or agent but not in the City’s name.

| | <u>Fair Value</u> | <u>Risk Category</u> |
|--------------------------------------------|-----------------------|--------------------------|
| Pooled investments held by City Treasurer: | | |
| U.S. Government Securities | \$ 2,316,432 | Category 1 |
| Investments held in trust: | | |
| U.S. Government Securities | 1,054,125 | Category 2 |
| Pooled and held by City Treasurer: | | |
| STAR Ohio | <u>1,689,347</u> | Uncategorized |
| | \$ <u>5,059,904</u> | |

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. The classification of cash and cash equivalents (deposits) for purposes of this note are based on criteria set forth in GASB Statement No. 3. A reconciliation between GASB Statements No. 9 and No. 3 follows:

| | <u>Cash and Cash Equivalents/ Deposits</u> | <u>Investments</u> |
|----------------------|----------------------------------------------------|--------------------|
| GASB Statement No. 9 | \$ 4,147,893 | 3,370,557 |
| Investments: | | |
| STAR Ohio | <u>(1,689,347)</u> | <u>1,689,347</u> |
| GASB Statement No. 3 | \$ <u>2,458,546</u> | <u>5,059,904</u> |

3. ACCOUNTS RECEIVABLE

Receivables at December 31, 2002 consist of the following:

| | |
|-------------------------------------------|--------------------------------|
| Earned and unbilled consumer accounts | \$ 2,506,492 |
| Earned and billed consumer accounts | 4,756,227 |
| Less allowance for uncollectible accounts | <u>(2,578,234)</u> |
| Total | \$ <u><u>4,684,485</u></u> |

4. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2002 was as follows:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|-----------------------------------------------------|---------------------------------|-----------------------------|----------------------------|------------------------------|
| <i>Capital assets not being depreciated:</i> | | | | |
| Land | \$ 92,101 | - | - | 92,101 |
| Construction in progress | 443,346 | 435,592 | - | 878,938 |
| Subtotal | <u>535,447</u> | <u>435,592</u> | <u>-</u> | <u>971,039</u> |
| <i>Capital assets being depreciated:</i> | | | | |
| Buildings and improvements | 418,587 | 24,701 | - | 443,288 |
| Machinery and equipment | 56,316,247 | 619,201 | (102,097) | 56,833,351 |
| Subtotal | <u>56,734,834</u> | <u>643,902</u> | <u>(102,097)</u> | <u>57,276,639</u> |
| Totals at historical cost | <u>57,270,281</u> | <u>1,079,494</u> | <u>(102,097)</u> | <u>58,247,678</u> |
| Less accumulated depreciation: | | | | |
| Buildings and improvements | 147,958 | 15,072 | - | 163,030 |
| Machinery and equipment | 17,935,637 | 1,756,115 | (54,740) | 19,637,012 |
| Total accumulated depreciation | <u>18,083,595</u> | <u>1,771,187</u> | <u>(54,740)</u> | <u>19,800,042</u> |
| Capital assets, net | \$ <u><u>39,186,686</u></u> | <u><u>(691,693)</u></u> | <u><u>(47,357)</u></u> | <u><u>38,447,636</u></u> |

5. RESTRICTED ASSETS

Restricted assets consist of assets whose use has been restricted by bond indenture, City Charter or City Council ordinance for debt service or gas rate stabilization. Restrictions and related assets are as follows:

| | | |
|--------------------------|--------|-----------------------------|
| Debt service | \$ | 251,372 |
| Reserve for debt service | | 1,528,201 |
| Gas rate stabilization | | <u>1,799,972</u> |
| Total | \$ | <u><u>3,579,545</u></u> |

6. LONG TERM DEBT

Long-term debt consists of Gas System Revenue Bonds issued in 1993, due serially through 2018 with interest from 3.2% to 5.15% per annum. Activity for the year ended December 31, 2002 was as follows:

| | Balance January 1, <u>2002</u> | <u>Additions</u> | <u>Reductions</u> | Balance December 31, 2002 | Due Within <u>One Year</u> |
|------------------------------------------------|--------------------------------------|------------------|-------------------|---------------------------------|----------------------------------|
| 1993 Series A Bonds | \$ 16,945,000 | - | (670,000) | 16,275,000 | 695,000 |
| Less deferred amount for issuance discounts | <u>(548,010)</u> | <u>-</u> | <u>(44,302)</u> | <u>(503,708)</u> | <u>-</u> |
| | <u>\$ 16,396,990</u> | <u>-</u> | <u>(714,302)</u> | <u>15,771,292</u> | <u>695,000</u> |

Under the terms of the revenue bond indenture, the City has agreed to certain covenants including, among other things, maintaining revenue levels and providing for operating expenses and debt service. The 1993 Series A Bond are insured under a municipal bond insurance policy. Under the terms of this policy, the insurer guarantees the payments of principal and interest.

Annual debt service requirements to maturity for the revenue bonds are as follows:

| | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|-----------|--------------------------|----------------------|-----------------------|
| 2003 | \$ 695,000 | 805,580 | 1,500,580 |
| 2004 | 730,000 | 775,000 | 1,505,000 |
| 2005 | 760,000 | 742,150 | 1,502,150 |
| 2006 | 795,000 | 707,190 | 1,502,190 |
| 2007 | 835,000 | 669,825 | 1,504,825 |
| 2008-2012 | 4,835,000 | 2,684,189 | 7,519,189 |
| 2013-2017 | 6,195,000 | 1,319,180 | 7,514,180 |
| 2018 | <u>1,430,000</u> | <u>71,500</u> | <u>1,501,500</u> |
| Total | <u>\$ 16,275,000</u> | <u>7,774,614</u> | <u>24,049,614</u> |

7. DEFINED BENEFIT PENSION PLAN AND OTHER POSTEMPLOYMENT BENEFITS

The City contributes to the Public Employees Retirement System of Ohio (PERS), a cost-sharing multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost of living adjustments, and death benefits to plan members and beneficiaries. The authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. PERS issues a stand-alone financial report that may be obtained by writing to PERS, 277 East Town Street, Columbus, Ohio 43215-4642.

The Ohio Revised Code provides statutory authority for employee and employer contributions. Plan members, other than law enforcement and public safety employees, are required to contribute 8.5% of their annual covered salary. The City was required to contribute 13.55% of covered payroll for employees. The Gas System's required contributions to PERS for the years ended December 31, 2002, 2001, and 2000 were approximately \$125,000, \$96,000 and \$63,500 respectively, equal to the required contributions for each year.

PERS provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit and to primary survivor recipients of such retirees. Health care coverage for disability recipients is available. The health care coverage provided by the retirement system is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. A portion of each employer's contribution to PERS is set aside for the funding of postretirement health care based on authority granted by State statute. The 2002 employer contribution rate was 13.55% of covered payroll for employees and 5.0% was the portion that was used to fund health care for the year.

The assumptions and calculations below were based on the System's latest Actuarial Review performed as of December 31, 2001. 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 2001 was 8.00%. An annual increase of 4.00% 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 4.00% base increase, were assumed to range from 0.50% to 6.30%. Health care costs were assumed to increase 4.00% annually.

The OPEB's are advance-funded on an actuarially determined basis. The number of active contributing participants was 402,041. The portion of the Gas Systems's contributions that were used to fund postemployment benefits was approximately \$46,000. At December 31, 2001, the actuarial value of the Retirement System's net assets available for OPEB was \$11.6 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$16.4 billion and \$4.8 billion, respectively.

8. CONTINGENT LIABILITIES

Various claims and lawsuits are pending against the City involving the Gas System. The City believes that the ultimate disposition of such claims and lawsuits will not have a material adverse effect on the financial position of the Gas System.

9. RELATED PARTY TRANSACTIONS

The Gas System sells gas to the City's Electric System for use in the generation of electricity. Revenues of approximately \$461,000 from the Electric System to the Gas System are included in operating revenues in 2002.

The City allocates the cost of certain administrative services. In addition, the City established internal service funds that provide services to various City departments. Charges to the Gas System for these services were approximately \$2,189,000 in 2002 and are included in other operating expenses.

10. PARTIAL IN-SUBSTANCE DEFEASANCE

In December, 2000, the City entered into an Escrow Trust Agreement with Fifth Third Bank. The agreement required that the City deposit \$8,265,000 into an irrevocable trust with the bank for payment to final maturity of \$8,265,000 of the 1993 Gas System Revenue Bonds. The funds deposited were used to purchase U.S. Government Securities, the principal of which, together with interest earned thereon, will be sufficient to pay, when due, the principal on such bonds. Principal payments on the in-substance defeased portion of the 1993 Gas System Revenue Bonds are not scheduled to begin until the year 2019.

11. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts and liability, damage to and theft of or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City maintains comprehensive insurance coverage, for all City departments including the Gas System, with private carriers for real property, building contents, vehicle, property and general liability insurance, police professional liability, and public officials errors and omissions insurance. Vehicle policies include liability coverage for bodily injury and property damage. Claim payments have not exceeded coverage in the past three years. There was no decline in the level of coverage from the prior year.

12. CONTRACTUAL COMMITMENTS

At December 31, 2002, the Gas System had contractual commitments to purchase gas from Noble Gas Marketing in the amount of \$3,244,430.

13. SUBSEQUENT EVENTS

Dated April 30, 2003, the City of Hamilton issued Gas System Revenue Refunding Bonds intended to provide, in conjunction with an irrevocable escrow trust agreement with Huntington National Bank, for the advanced refunding and in-substance defeasance of the existing 1993 Gas System Revenue Bonds. The bonds were issued with a face value of \$14,540,000 and included the purchase of U.S. Government securities that when combined, with interest earned thereon, is considered sufficient to provide for an in-substance defeasance of the existing 1993 Gas System Revenue Bonds. The City also liquidated available bond funds and the debt service reserve fund of the 1993 Gas System bonds to provide for the advanced refunding.



Clark, Schaefer, Hackett & Co.
CERTIFIED PUBLIC ACCOUNTANTS
BUSINESS CONSULTANTS

Honorable City Council
City of Hamilton! Ohio

We have audited, in accordance with auditing standards generally accepted in the United States of America the statement of net assets of the City of Hamilton! Ohio - Gas System, (Gas System) as of December 31, 2002, and the related statements of operations and cash flows for the year then ended, and have issued our report thereon dated June 16, 2003.

In connection with our audit, nothing came to our attention that caused us to believe that the Gas System failed to comply with the terms, covenants, provisions or conditions of Sections 5.2, 5.5, 5.6, 5.12, and 5.13 of the Indenture dated October 1, 1993 with Fifth Third Bank, trustee, insofar as they relate to financial and accounting matters. However, our audit was not directed primarily toward obtaining knowledge of noncompliance with such Sections.

This report is intended solely for the information and use of the City Council and management of the City of Hamilton! Ohio, Auditor of State of Ohio, and U.S. Bank and is not intended to be and should not be used by anyone other than these specified parties.

Clark, Schaefer, Hackett & Co.

Cincinnati, Ohio
June 16, 2003



**Auditor of State
Betty Montgomery**

88 East Broad Street
P.O. Box 1140
Columbus, Ohio 43216-1140

Telephone 614-466-4514
800-282-0370

Facsimile 614-466-4490

CITY OF HAMILTON - GAS SYSTEM

BUTLER 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
AUGUST 26, 2003**